103

A SHOT IN THE ARM FOR OREGON'S ECONOMY: MAKING CREDIT AND CAPITAL MORE AVAILABLE TO SMALL BUSINESSES

HEARING

BEFORE THE

SUBCOMMITTEE ON REGULATION, BUSINESS OPPORTUNITIES, AND TECHNOLOGY

OF THE

COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES

ONE HUNDRED THIRD CONGRESS

FIRST SESSION

PORTLAND, OR, TUESDAY, JANURY 12, 1993

Printed for the use of the Committee on Small Business

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A SHOT IN THE ARM FOR OREGON'S ECONOMY: MAKING CREDIT AND CAPITAL MORE AVAILABLE TO SMALL BUSINESSES

TUESDAY, JANUARY 12, 1993

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON REGULATION, BUSINESS
OPPORTUNITIES, AND TECHNOLOGY,
COMMITTEE ON SMALL BUSINESS,
Portland, OR.

The subcommittee met, pursuant to notice, at 9:40 a.m., at Northwest Natural Gas Co., 220 Northwest Second, Portland, OR, Hon. Ron Wyden (chairman of the subcommittee) presiding.

Chairman WYDEN. The subcommittee will come to order.

Today, the Small Business Subcommittee on Regulation is especially pleased to be able to join with our new member of the Oregon congressional delegation, Congresswoman Furse.

I would like to take special note and take special pride in the fact that this is the first formal hearing that Congresswoman Furse has attended, and it gives me special pleasure to be able to welcome her.

I think that the members of the Oregon congressional delegation, in particular those who are going to be faced with the challenge of creating jobs, are especially fortunate to have Congresswoman Furse as our first member on the Banking Committee for some time.

I will have a short opening statement, and Congresswoman Furse will have one, as well, but if champagne glasses were allowed at Small Business hearings, we would certainly be tinkling them now, because we are especially pleased to be able to have Congresswoman Furse as part of our delegation. She is going to be in a very good position to address a lot of the issues that we are going to be bringing up today.

Today, the Small Business Subcommittee on Regulation is going to examine new strategies for making available more credit and capital to Oregon's small business.

Recent evidence shows signs of a national economic rebound, but for Oregonians, the real key is to produce new jobs that pay good wages.

Too often, we have seen in the past that large companies have grown by streamlining their operations and actually reducing their workers.

For small business, we have seen just the opposite. Growth there does translate into more jobs.

Clearly, the task of creating more jobs can be dramatically affected by the small- and medium-size business sector, and I think we all know that this is especially the case here at home.

Over 90 percent of Oregon's businesses employ fewer than 100 workers. The State Division of Employment projects that about 70 percent of the job creation in our State during the 1990's is going to come from small firms.

So, the challenge for Congresswoman Furse and me is straightforward: Make more money available to small- and mid-size businesses, and we grow jobs in Oregon; sit on our hands, and we can lose our life blood.

We choose the growth option and want to use this hearing to promote just this sort of economic growth agenda.

Traditionally, the responsibility for lending to small businesses has fallen to local banks. In return for guaranteed deposits and borrowing rights, the Government has expected banks to make special efforts to contribute to the economic health of the local community.

Indeed, the Community Reinvestment Act of 1977 formally requires that banks demonstrate that the efforts they make to meet the credit needs of the local community show loans for small business and housing.

Here in Oregon, activists working with the financial institutions have clearly made progress with the Community Reinvestment Act on the housing side of the ledger. We wish to see the same sort of progress made on the small business side.

Oregonians want the Community Reinvestment Act. It is a powerful tool for economic growth and not a paperwork nightmare for bankers or a full employment act for regulators.

Too often, the rules and standards that regulate financial practices defy reality. Yesterday, I spent an hour at Key Bank headquarters in Portland and saw the loan officers have to fill out a mountain of paperwork just to make a loan.

A recent edition of Associated Oregon Industries Business Viewpoint reports, "A customer who has a First Interstate account in Vancouver can use an automatic teller machine or cash a check in a First Interstate branch to get cash but cannot make a deposit to the Vancouver account in Oregon."

Clearly, there is much to do in getting rid of such mindless regulations.

Now, depending on who you talk to, there are a variety of reasons why small business finds it hard to get capital.

The Chair does want to take note of the fact that the experts have reported that, in 1992, for the first time since World War II, America's banks actually invested more money in Government securities than they lent to businesses.

We also wish to take note of the fact that Oregon's largest banks have performed significantly better than the national average on this issue.

The records obtained by the subcommittee from the Federal Deposit Insurance Corporation indicate that, even here at home, the three largest banks decreased commercial loans by $272 million and increased investments in Government securities by $725 million in the last year.

Now, the fact is that what our community needs is a new partnership to mobilize our State to work with the Clinton administration to implement the President-elect's pledge to increase small business lending.

Toward that end, Congresswoman Furse and I intend to put together a working group at the conclusion of this hearing to work for an Oregon growth agenda that the two of us can pursue with our colleagues, and we will have a special opportunity with Congresswoman Furse's key position on the Banking Committee to have her work with our delegation in pursuing this agenda.

We do have significant tools at our disposal. The Small Business Administration has indicated that they wish to be an activist partner in promoting this kind of coalition. Portland State University wants to help the emerging businesses.

So, we look forward to our witnesses and the important follow-up work that lies ahead. Now, I want to recognize, with special pleasure, our new member of the Oregon congressional delegation, for her opening statement at her opening hearing, Congresswoman Furse.

[Chairman Wyden's statement may be found in the appendix.]

Ms. FURSE. Thank you so much.

I would particularly like to thank Chairman Wyden for inviting me to participate in this hearing, and I would like to thank you for coming at this early time in the morning to educate me and us, and I stress the word "educate," because I have actually, right now, at this moment in time, been a Congresswoman for exactly 7 days.

So, I need to learn a great deal, and I am eager to learn.

I want you to know I do not come with any particular predispositions in regard to the Community Reinvestment Act.

Chairman Wyden has invited me here, I believe, both for my membership on the Banking Committee and on the Housing and Urban Affairs Subcommittees, and because, together, we represent the economic heart of Oregon. But there are a couple of predispositions, or one at least, that I do bring to the hearing, which is that I am a small business owner myself.

My husband and I own a vineyard in Washington County. So, I know firsthand some of the things you have to do to obtain some financial support, and I am aware of the problem of overregulation.

I feel I have some understanding of what it is to be on the banker's side of the lending process, seemingly endless regulation, voluminous paperwork, and so, I want to learn more about your needs and your concerns.

As I traveled through the First District during my campaign, I came to realize there were two very important things going on in the First District: The need to stimulate and support expansion of small business in Oregon, especially in high-technology and electronic companies, which really do play a huge role in our economic life, and the second thing I learned over and over was the need for affordable housing in the First District and, I am sure, in the whole of Oregon.

Because these needs are so important, that is why I sought and, I am glad to tell you, I obtained membership on those two very im-

portant subcommittees, Housing and the Consumer Affairs Subcommittees.

Of particular concern to me is the need for the high-technology industry of Oregon to get loans and working capital.

So much of our economic health is dependent on the ability of high-technology and electronic firms to grow and take advantage of new technologies. That is very important to me, to you, and to that industry.

I understand that the climate of investment is changing, but there is still need for improvement, and perhaps the biggest need is the need to educate ourselves, both the banking community and the high-technology community, of the special needs of that community, and I think that is something we can work toward.

There are many emerging new and exciting technologies, and one of those things that I think we need to look upon is how do we support the development of environmental technology?

That is a $370 billion-industry globally, and I think that we in Oregon need to be on the cutting edge of that. That is an effort which will pay handsome dividends in our State.

So, Mr. Chairman, I want to hear what our panelists have to say and hope we can begin a dialogue, begin a meeting of minds as to how, under these uncertain economic times, enough capital can be safely provided to our small businesses so that they can flourish and survive, for they are truly the life blood of our communities.

Thank you, Mr. Chairman.

[Ms. Furse's statement may be found in the appendix.]

Chairman WYDEN. I thank my colleague for a fine statement, and this is going to be one of the priority issues for our session, and I look forward to our follow-up efforts, as well.

Let us bring our first panel forward, Herb Shaw of the Laughlin Group, Matt Chapman, and Mr. William Naito, to outline and describe for us some of the problems faced by small businesses in securing capital.

If you three will come forward, it has always been the practice of the Small Business Subcommittee on Regulation to swear all the witnesses who come before the subcommittee. Do any of you have objection to being sworn as a witness this morning?

Please rise and raise your right hand.

[Witnesses sworn.]

Chairman WYDEN. We welcome all of you and have had the pleasure of working with each of you on a variety of community initiatives in the past. If you would, in the interest of time, take about 5 minutes or so to summarize your principle concerns, that would be helpful.

We will then have questions with Congresswoman Furse beginning. Why don't we begin with you, Herb? We have to use, I am told, that lapel microphone, if it can be passed around.

TESTIMONY OF HERB SHAW, PRESIDENT & CEO, LAUGHLIN GROUP OF COMPANIES

Mr. SHAW. Well, good morning, Congresswoman Furse and Congressman Wyden. We appreciate this opportunity to be with you

and to testify on behalf of the small business community in Oregon.

Let me state very quickly, I am a small business owner. I have been the CEO and president of several companies in Oregon and elsewhere.

As I think some of you know, I have been a venture capitalist in Portland and have invested in a number of small businesses, primarily high-technology companies, and so, we are very much aware of the need in this community.

My message today is very clear. We are talking about debt and, for the most part, lending practices. I would like to talk a little bit about the other side of the financial picture, and that is the formation of equity capital for the small businesses.

At some point, a small business cannot afford to continue to load themselves with debt, and there comes a time when permanent capital is required. We think that there is a need in this community, as well as elsewhere, to provide funds for that purpose.

I want to distinguish between venture capital and the kinds of funds that we're talking about. Venture capital, for the most part, is invested in very, very young companies, very high-risk, with the hope that there is a high reward.

There are multitudes of companies that are already established. They are small, looking for growth, have less of a risk at this point in time, and probably have less of a reward at the end for their investors, but, nonetheless, they provide a significant number of jobs for this community.

We think that you must balance the debt as well as equity in any sort of growth scenario. We have proposed to Congressman Wyden's office a fund that might provide for this, akin to a venture fund.

We would support the formation of a fund that would be used across the country in each State that would be partially funded by Federal funds as well as private funds.

This—call it the entrepreneurship fund if you will—is established to be able to put money into these small companies that are already in business and are looking for additional capital for growth purposes. I will give you one example.

There was a company in town here that we know quite well. They sold lawn ornaments and things of that nature. I was shown a purchase order on the desk for an amount close to $2 million that would put this company in a completely different set of circumstances.

They could not fulfill the order. They could not find the working capital required to accomplish that, and, as a consequence, they are as small as they were a year ago. They could have provided additional jobs and what have you.

The fund that we are talking about is very simply this: We think that money can be made available, both private as well as Federal funds, to be administered through one of the agencies in the Government, but frankly, we would like to see that as a pass-through.

The funds would then be administered within each State by a board of trustees or a board of advisers, who then would give that money, through bids if you will, to money managers or portfolio managers.

These people would then look for these opportunities within the community and be able to provide the capital for that. Again, this would be equity participation. That is what we would like to see happen in this community.

Thank you.

Chairman WYDEN. Mr. Shaw, very helpful, as always. We will get through our panel members first, and I know there are some questions.

Bill Naito, welcome.

TESTIMONY OF BILL NAITO, PRESIDENT, NORCREST CHINA CO.

Mr. NAITO. It is very nice to be able to talk to the people who really run this country in the beginning of the new year and a new term.

I just want to give a short bio of myself in relationship to small business. I supply a lot of office and store spaces to small businesses, and I think we have about 250 tenants. Some are very small, and some are a little larger.

The other area in which we do involve ourselves in small business in the State is a very important one, and that is through our Made-In-Oregon stores. That has become nearly a $10-million business here. We buy from over 3,000 vendors, and they are very small ones. The largest one is Pendleton, and these small businesses aspire to be, eventually, a Pendleton or like Nike shoes, but the past 3 years, I have never heard so many complaints that, sure, they have this wonderful jam or a myrtlewood figure, but they do not have enough money to finance their production.

So, you have wonderful things, but can you fill a $10,000 order? Well, have you tried the local bank? They are all loaned up or it's impossible to get funds from the banks.

These are very strategically located factories, because they are in places like Coos Bay or Drain, Oregon, or these small towns that are suffering right now from the timber problem, and here is the possibility for them not to move out of town but start a little enterprise there to get going and provide jobs, and, eventually, they will do well.

The same goes for the small businesses that I have watched through the Saturday Market, 350 small vendors there, and they eventually have become very successful craftspeople.

Another one, down in Old Town, is Daisy Kingdom, started out with just nothing, and now she does a sizable business nationwide. That catalog goes out, and she is now a consultant to Hallmark Cards in Kansas City. Those are some successful examples. There are a lot more.

Before, banks would supply the necessary capital to get it going—it is not equity but debt capital to get these small shops and small enterprises going—but today that's all cut out, and for 6 years, from 1980 to 1986, I was a director of a local Federal Reserve bank, and I used to lobby Mr. Volker to get the interest rate down, and Sandra Suran, on the next panel, she and I were on the board together, and we saw that interest rate, the prime, come from 21 down to, today, 6.

That is fine, but you cannot borrow the money at 6, 7, 8, 9, or 10, and the culprit, I think, is not the Federal Reserve.

Now, we have got to focus on the Office of the Comptroller of the Currency, OCC, the regulators there who make it impossible for banks to do their job in the community, their economic role, and I think you should get the Comptroller of the Currency and the regulators. I hear these horror stories directly from our bankers here. The other is this paperwork.

You need about an inch of paper, and before you needed two sheets. You should read Joe Weston's article in the apartment booklet or magazine. He says, before, he was able to carry on his apartment low-income housing or affordable housing with just two sheets of paper, and now it takes a book, and he quit. These horror stories are really true, because they come from all three banks or four banks, and I think that is a real problem today, and we need those small businesses.

If the regulators would allow the banks to loan money, that will create jobs faster than any public works program. It is a matter of months, and then you would change this whole economy around, the whole country's economy around, and especially here in the State of Oregon.

Thank you.

Chairman WYDEN. Well said, Mr. Naito.

Mr. Chapman.

TESTIMONY OF MATT CHAPMAN, CHAIRMAN AND CEO, CFI BANKERS SERVICE GROUP, INC.

Mr. CHAPMAN. Thank you.

I would echo the panelists in terms of my appreciation for a chance to be here this morning and also in terms of the importance of the issues that you are addressing.

My position as chairman and CEO of a company called CFI Bankers Service Group, Inc., which you have probably never heard of, although I want to also express my appreciation for scheduling the meeting, is the building we are headquartered in. So, I only had to go five floors to make the meeting.

CFI has a story that I think is probably very relevant to the kinds of the things that you are talking about, and I would like to spend a couple of moments and share it, because it, I think, is maybe an illustration of both Herb's and Bill's points.

We are a small business. We provide software to the banking industry for documentation and related services, and we are the eighth-largest supplier of the software to the banking industry nationwide, but we are still a small business.

We did a little over 15 million in sales last year; we have 130 employees.

Several years ago, we had the good fortune to have a very, very fine relationship, a lending relationship with our bank, but we were a high-technology company.

Our bank was both a customer of our company and a reverent supporter of our product line. We have the advantage of having a product that leads the market.

We have an experienced management team, a very, very positive cash-flow, but, at that time, our banker was told by the regulators that they needed to stop lending in the high-technology industry, and Congresswoman Furse, I am especially in agreement, for all the obvious reasons, with your comment of how important high-technology companies like ours can be.

Our company had approximately 20 employees 5 years ago. So, we have added 110 jobs to the Oregon economy within the last 5 years, and we did it, initially, with a line of credit from our bank.

It was an appropriate line of credit to our needs, and our banker was told that this was not the kind of loan that the regulatory agencies felt they should have.

The result, for us, turned out to be very, very fortunate. We had a very good relationship. The bank held off the situation for a year, referred us to a source of capital, what are known as mezzanine financing agencies.

It is not the venture capital groups that Herb referred to but groups that will put money into a company that is in a later stage of development, as we were at that time.

So, today, as I am here this morning, we are debt-free. We have several millions of dollars on deposit with our bank, but if our bank had not been willing to work with us during that time period and had not been willing to stand up to the regulatory agencies and say we believe in the management of this company, I would not be testifying in this capacity today, and I cannot over-stress how critical it is.

The other point I would make is what is really critical, in my view, to a small business, and Herb has said it very well, but I just can't resist echoing this.

There are two sides to the equation. Today, if you look at what is available through venture capital in Oregon, it is not a great deal.

A lot of the traditional companies have moved away. This is not a venture capital market for them, but even when they are here, even when they are well-funded, the reality is that a venture capital organization, appropriately, as Herb points out, is interested in early-stage companies that might become a Nike or they might become a Sequent or a Metagraphics.

There are very, very few organizations that do that, and they are not the source of most of the jobs.

The companies that need this kind of capital are companies like we were at that time, where we're not necessarily going to be a Nike or a Sequent or something like that. I mean that would be nice, but that is not the likely result for our company.

We will continue to grow, and we will continue to do well, but the fact of the matter is that we created jobs on an organization of steady, solid growth.

The banking industry was willing to provide us with the liquidity we needed but was told by the regulatory agencies that they could not do it, and those are the two sides of the issue. It is the regular, journeyman company that needs access to capital.

When we did our capital funding, we acquired a combination of available debt and capital of $7.1 million. It cost us $400,000 in fees and took a year to get it.

The fact of the matter is that, if we had been able to tap capital sources earlier, we would have had far less in the way of fees, we would have been able to grow much more rapidly than we had one, and we were very much like the story that Herb described, where there were areas in which we could fulfill the orders on business because we just, frankly, could not cash-flow the issue. The combination of available capital to the journeyman company, together with letting bankers make the determination as to whether the character and the management of a company deserves their support, are the two issues that I would commend to the committee's consideration, because I think those two things will make the difference in making credit and capital available to companies such as ours and the others that are represented here today.

Thank you.

Chairman WYDEN. Very interesting.

Ms. Furse, do you have questions?

Ms. FURSE. Yes.

I know that the Oregon Bankers Association has an excellent plan of seminars when they do lending to new homeowners. Do you think there is a need for that kind of assistance for small business?

I am thinking in terms of just how to run a company and what might be pitfalls. Can the banking industry help in that way?

Mr. SHAW. To answer the question, what is also missing, aside from capital, we think, in some small businesses, is the need for management help.

In a lot of cases, the entrepreneur has been schooled in perhaps the technologies and may not be schooled in marketing techniques and what have you.

We think it is very important that, along with capital, we have this educational process or, in fact, direct help. The banks could play an enormous part in that in at least a seminar forum.

I think the banks have to be—and I think they are—careful. They cannot run somebody else's business, and that is not what they are trying to do, but I think they could play a part in at least the education process, certainly.

Mr. CHAPMAN. Let me echo that, because also I think there is a void.

Theoretically, the role that you talk about would be filled by the Small Business Administration, and before I took the job I have now, I used to practice law, which meant, essentially, I did not know anything about running a business.

So, the result is that, when I changed positions, I was looking for what would be available to learn those kinds of skills. I was extremely disappointed, to be very candid, in what was available through the Small Business Administration.

What is interesting to me is that the one course I found that was of value was offered by one of Oregon's larger banks, and I found that to be of considerable help, but I would echo Herb's comments.

I think that the educational function is there, but what is important to recognize is that, for example, when we sat down with our bank and worked through the conditions of the loan and all of that type of stuff, one of the things the bank said, they were not going to tell us how to run the business, but they were telling us that we better have a business plan, and until we presented a business plan

to them that was an acceptable, realistic plan, they were not interested in talking to us, and I will tell you, that can be an absolutely terrific discipline.

Mr. NAITO. Well, the Portland Chamber does a pretty good job in their small business seminars, and later you will hear from Carl Flipper, Oregon Enterprise Forum. The other day he called me with an idea for this man down in Oregon City with what's called enoki items, and how to get financing for it, but it could be formalized, and the banks could have seminars in how to get funds.

Ms. FURSE. Thank you.

Chairman WYDEN. Well, all of you have been great. Just a couple of quick questions.

Is part of this problem possibly that these loans for banks simply are not as profitable as other kinds of loans, where they are larger, and the revenue involved is simply much bigger, and they are likely to be more profitable?

Mr. CHAPMAN. Actually, my experience is the very opposite, that, in fact, if you look within our customers, we serve about 2,000 banks throughout the country, and, so, we pay some attention to these kinds of issues.

It is certainly true that the loans to companies such as ours are smaller, but the bank is, in fact, in a position to command a little bit better rate.

The very large loans, by and large, are no longer made by the banks.

If you look at a study, for example, by the Arthur Anderson organizations, one of the best that has been done, called Vision 2000, one of the things they point out is that 75 percent of the volume of loans done in this country are now done outside the commercial banking industry, and when a large number that is in good shape needs money, they go direct to their commercial paper markets, and they do not need the banking industry as much as they used to for that particular function.

So, the source of funding for small businesses is, and I think should be, banks, and the irony of the thing is that I think if you looked and got behind bankers' statements—I see that some of the bankers are here—I think you would find that this is a very, very profitable line of business for them in terms of small business loans, but their concern that has been expressed to me in terms of our company has been whether or not the kind of loan they are making is going to meet the kind of ratio analysis and whether or not they cannot make the kind of loans based on the character or their belief in the company anymore, but I do not think it is a profit problem.

Chairman WYDEN. The only thing that comes to mind is, if these are profitable loans, you would ask why more are not being made.

There certainly seem to be a lot of mindless regulations, and Congresswoman Furse and I want to get rid of those, and second, you get to the question of, given those regulations and the overall picture, is it profitable, and if it is profitable, even in spite of some of these mindless regulations, we have to ask, again, how come we are not getting more made.

Mr. NAITO. Profitability is probably the answer, but these regulations, the amount of time required, I guess it is not worth their time and effort to process some of these loans.

So, what I would like to have Congress do is talk to the OCC and straighten them out, because we have a nationwide banking system, and the regs come from the Office of the Comptroller of the Currency, and if you could straighten them out, it would filter down to your favorite State.

Chairman WYDEN. Well, one of the reasons we want to have this working group is to try to get as specific as we can—and we are going to ask the bankers this when they come up—on what we all agree are these horror stories, these regulatory nightmares, so that we can try to isolate as many of the specific ones as we possibly can, and then, as Mr. Naito correctly suggests, get to the regulators and see what could be done to change them.

The only other question I have is, and maybe Mr. Shaw is a good one to ask, in your opinion, what ought to be done to make the SBA more effective? Matt Chapman talked, I think correctly so, about some of the cautiousness in the nature of the lending practices at SBA?

Mr. Shaw, do you have some thoughts on what could make the SBA a more effective advocate?

Mr. SHAW. Well, I do. This is a subject that we have talked about before.

I think the first thing that I would do would be to take a look at the leadership within SBA and change that leadership out to include people who are business people, who have had business experience, who have gone through the kinds of things that we have all gone through, and who understand at the very grassroots level what it means to apply for a small business loan and so on.

I think, if you started at that point, the SBA would be truly an advocate of small business. As it is today, it is a functionary organization carrying out certain kinds of things that, at this point in time, we find less useful than perhaps at any other time.

I think, this is tough to do, but if you are able to reorganize it in that fashion and be able to inculcate the people who man that organization in the ways of business—and I do not think that is too terribly far apart from the real purpose of SBA—that might be the answer to it.

Chairman WYDEN. Well, we have not talked about an area that I am going to zero in on this session. We are fortunate to have Congresswoman Furse on the Banking Committee. I chair a Small Business Subcommittee.

I am very much of the view that now is the time for an overhaul at SBA. I think we have got to get some of those folks out of Washington.

I think we have got to get them closer to local communities, doing the kind of hands-on advocacy that you are talking about in terms of really understanding what it is going to take to make loans and to make loans other than, as Mr. Chapman correctly points out, in very limited, cautious kinds of circumstances.

So, we will ask our working group for some suggestions in that regard. When the bankers come up, we will try to get some more

specificity on the horror stories. We excuse you and thank you for the good work.

Thank you.

Our next panel can tell us of regulatory burdens and paperwork that our banks face. Mr. Frank Brawner, Oregon Bankers Association; Mr. William Humphreys of Madras; Mr. Winnowski, president of Key Bank; and Mr. Morry Burford of First Security Bank, Salem.

As the table collapses under all those forms, we will see if Northwest Natural Gas will pay the bureaucracy bill.

We welcome all of you. Thank you.

We do make a practice of swearing all our witnesses who come before the subcommittee. Do any of you have any objection to being sworn?

Please raise your right hand.

[Witnesses sworn.]

Chairman WYDEN. We welcome you and thank you for your cooperation. All of you have been very helpful to my office and to Congresswoman Furse's office.

Mr. Brawner and I talked late last night about the working group. I wish to commend him for his cooperation and willingness to pursue that with Congresswoman Furse.

We welcome you, Mr. Brawner. Why don't you begin?

TESTIMONY OF FRANK E. BRAWNER, PRESIDENT, OREGON ASSOCIATION OF BANKERS

Mr. BRAWNER. Chairperson Wyden, Congresswoman Furse, on behalf of the Oregon Bankers Association, we thank you for this opportunity.

My name is Frank Brawner. I am with the Oregon Bankers Association. I would like to give to you a packet that we have prepared. We are just going to mention what is in the packet briefly.

There is one good feature of the regulatory burden. A great deal of paper is used, and paper comes from Oregon. So, from that standpoint, that is the only benefit.

In the packet, you will find the brochure that we have prepared that quantifies the amount of burden. It is the theme of our campaign. The first week in February, nationally, we are calling "Cut the Red Tape, Let Banks Get Back to Business" Week.

We hope that you will have an opportunity to look at the graphs and the documentation contained.

On the left-hand side of the packet is Mr. Burford's testimony on June 19, 1992, in San Francisco before the Federal Financial Institutions Examination Council.

This is the result of a survey that we completed, about 6 months of work, getting input from all of Oregon's banks.

Now, let me tell you that contained in the FDIC Improvement Act, Congressman Wyden, as you know, was a provision that this council would study the regulatory burden.

That has been released to the Congress. It is dated December 17th, and the data contained in there would argue with the conclusion that we in the industry have come to.

We believe that the cost of the regulatory burden is $10.7 billion nationally. By the way, that converts to an Oregon cost of $105 million. They say no, it is $17 ½ billion.

They also go on to quantify——

Chairman WYDEN. A lot of money by anybody's calculation.

Mr. BRAWNER. It does not matter. When you start using B's, I do not understand.

Here are some comments from this study, and Congresswoman Furse, your committee has copies of this, as I believe all the offices, and this will be an item, I am told, that will be discussed by Chairperson Gonzalez rather soon.

It says that we regulate to the lowest common denominator, and we legislate to the lowest common denominator. We know that.

Oregon banks are regulated and legislated for the faults of others in other parts of the country. Well-run banks are treated just the same as those that are not as well run.

Examiners, it says in here, have zero tolerance and that examiners try to micromanage the banks.

Well, that study will speak for itself, and I am tickled that study is available to you, because it comes from another party, and it comes from the examiners themselves.

Let me say that on the right-hand side of your packet is a press release on top that indicates our computation of $10.7 billion.

By the way, another figure there that is very important is that converts to 59 percent of the profit of banks; 59 percent of out profit goes for the regulatory burden.

Let me go through the rest of the material that is here.

The next page, "Our Bank Regulatory Burden: A Mounting Problem," points out that no other industry is as heavily regulated, that over 40 major regulatory provisions have been adopted by the Congress since 1987, and that 41,000 bank employees spend their entire day dealing with compliance.

The next page gives you a list of 34 major provisions adopted in the last 5 years.

The next page talks about safety and soundness. I want to assure both of you and the audience that nothing that we are talking about deals with safety and soundness. There is no replacement.

We do not intend to suggest even the slightest rollback with regard to safety and soundness of America's banks, but let me tell you, in my opinion, safety and soundness is now affected because of the regulatory burden.

It is becoming a safety and soundness issue, because banks are so heavily regulated.

Why do banks invest in Government securities rather than make loans? Because you do not have a critical examiner, because you do not have a regulatory burden, because it is safe, it is easy, and no one is going to criticize it.

Not every bank, by the way, has the capacity to stand up to a regulator, as the previous panel member, Mr. Chapman, suggested, because not every bank has the capital within their means to do so.

The safety and soundness protections that we are listing there stay in place, and we do not even touch those.

Finally, there is a survey of the regulatory burden and a summary of the results.

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The final page that you will find in your packet, Mr. Chairperson and Congresswoman Furse, are the specifics. This has been a State association initiative with the American Bankers Association nationwide.

Here are 32 specifics that we would hope to introduce as legislation the first week in February, during our "Reduce the Burden" Week. There are 32 specifics here that have come from across the country, with Oregon input as well.

I look forward to working during this session of Congress to see if we cannot get banks back to business, to making loans.

Chairman WYDEN. Very good and very helpful. We will have questions in a moment.

Mr. Winnowski.

TESTIMONY OF T.R. "TED" WINNOWSKI, CHAIRMAN AND CEO, KEY BANK OF OREGON, AND CHAIRMAN-ELECT OF OREGON BANKERS ASSOCIATION

Mr. WINNOWSKI. Thank you, Congressman Wyden, for the opportunity to be part of this panel, and thank you, also, Congresswoman Furse, and any other members of the panel, for their interest in what is a timely subject.

My name is Ted Winnowski, and I am chairman and CEO of Key Bank of Oregon and the chairman-elect of the Oregon Bankers Association.

Key Bank of Oregon is a subsidiary of a $25-billion corporation, but it is a series of community banks, and we have 71 branches in this State and more than $1.7 billion in assets.

Key Bank of Oregon and other banks throughout the country want to serve our small business customers, but there are issues that affect the level and quality of this service.

The issue is not that the money is not available. The issue is not that the need is not there. In fact, the element of supply and demand is there. What are some of these issues? From our perspective, there are several.

The recent recession has left many small businesses undercapitalized, perhaps not well managed, and in jeopardy. Small businesses are turning to banks for help. Banks want to help but are discouraged by what they discover.

A small business may seek new venture capital assistance but not have any equity for the initial investment, or the principle may not have any experience, or there may not be a workable business plan.

While banks are working with small businesses on these issues, they are also having to deal with many issues related to their ability to provide credit for a small business.

Today, I want to focus on what the banking industry has found to be some of the largest obstacles in providing quality credit services to small businesses. Among these are the regulatory and administrative burdens.

Our own Key Bank loan officers continually ask how can I comply with all these regulations and paperwork and still deliver the services small businesses need at a reasonable cost and within a reasonable length of time?

The effects of these burdens translate into increased costs, as have been outlined by our earlier panel members, and increased red tape for both the bank and the small business customer.

The increased cost and time can affect the delivery of certain services or even eliminate some.

At Key Bank, we no longer transact adjustable-rate mortgages due to the complexity of the disclosures. The complexity makes the potential for error and, consequently, the potential for a penalty unusually high.

Though you may not think the loss of adjustable-rate mortgages would impact small business, it certainly does. Home equity may be the only asset available to fund a new business venture.

While the new business ventures may be affected by lack of adjustable-rate mortgages, established small businesses face expansion obstacles.

The Federal Insurance Reform, Recovery, and Enforcement Act, FIRREA, or diarrhea if you would like, requires appraisals or evaluations of every real-estate-secured loan, a process that required Key Bank to increase our appraisal staff from one to three people.

A collateral appraisal for a $500,000 loan cost $1,700 5 years ago. Now, the least-expensive appraisal under current regulations costs $5,500.

In addition, another review of this original appraisal is called for, and a second report costing from $600 to $900 is also required.

Not only does the customer have to pay these costs in advance, but the bank cannot offer any loan commitment until the appraisal is completed and the property is qualified, taking as long as 3 to 5 months.

Let us address another regulatory problem affecting all small businesses, classification of loans.

A loan becomes classified when a regulator determines the bank is in danger of not receiving payments or does not meet the regulator's strict credit-quality standards.

Classification restricts our ability to meet the individual needs of small businesses, making the old-time creative lending no longer an alternative.

Although the foundation for Government regulations is to ensure safety and soundness in this banking industry, the fact is, for a bank to be safe and sound, it must also be profitable.

Today, efforts to maximize bank profitability and to fund small business loans can be at odds. Regulated capital requirements now make it more profitable for us to invest deposits in Government securities, as you have already elicited, rather than in small business loans.

Currently, one dollar invested in Government securities requires Key Bank or any bank to have 1 cent in reserve. Government securities, paying up to 7 percent interest, are basically risk-free.

The same $1 invested in a small business loan at, let us say, prime plus 1, prime plus 2, 6–7 percent or 7–8 percent, costs the bank an 8-cent reserve.

Which is the more prudent investment in the eyes of our depositors, in the eyes of our stockholders, or the FDIC?

It is interesting to note that unregulated investment companies do not have to comply with any of these rules, resulting in a rather unfair competition.

I regret banks' unfair reputation for not wanting to lend to small businesses. We have always prided ourselves at Key Bank on our commitment to small business, and I know a lot of our associates do, as well.

A year ago, we reorganized to better accommodate small loans. Today, each of our lending centers throughout the State has on its staff at least one lender who does nothing but deal with credits under $150,000.

It is becoming increasingly noticeable that the issues I have just outlined, and many others, are impacting both the health of small businesses and banks' ability to serve this important segment of our economy.

Here in Oregon, as has been cited, we have small businesses per capita than in any other State. Small business is actually becoming big business. What can we do? I would like to offer a few suggestions.

First, as Congressman Wyden has alluded to, create a small business committee or task force of major local bank regulators, bankers, and small business reps. This committee could examine these issues at a local level to develop Congressional recommendations.

Some of these recommendations might include creating an Oregon small business loan fund offering microbusiness loans under $20,000. This fund would be accessible to all entrepreneurs.

Currently, there are only a couple of very restrictive loan funds operating as this in Oregon, one being OAME, the Oregon Association of Minority Entrepreneurs. We think these compacts work.

The committee might also recommend such things as lowering bank capital requirements for small business loans.

It might recommend establishing a sophisticated borrower exemption from regulations like Reg. Z, truth in lending, and the Real Estate Settlement Procedures Act.

This exemption might allow individuals and businesses with assets, say, in excess of $300,000, to access funds on a more creative and competitive basis without all the hoops.

Some additional suggestions might be to design rules that level the playing field for banks, credit unions, and unregulated investment companies, to also address this appraisal and real property lending requirement to minimize the delays and costs involved in plant expansion and commercial construction.

Also, last, we would like to ask that you might require small business applicants who intend to rely on Government guaranteed programs, or maybe even some others, to complete a class, to complete a seminar, whatever it is, on management, understanding credit, and the application procedures.

It is important for us that potential customers be better prepared.

To move ahead, we need a realistic assessment of current banking regulations and their effect on the ability of small business to access bank capital. I think our earlier panel mentioned that very succinctly.

I am asking lawmakers, community leaders, and business representatives to recognize the overregulated barriers affecting the extension of commercial credit, to recognize the need for some intermediaries to function as consultants, helping entrepreneurs understand credit and credit requests.

We want to work with small business, we want them to succeed, and we need changes to do this.

We are among the banks, perhaps unlike others, that in this past year or two have grown their loan portfolio and decreased their securities portfolio. We look for the challenge to do even more on the loan side, and thank you for the opportunity to appear before you.

Thank you.

Chairman WYDEN. Mr. Winnowski, thank you for an excellent presentation, and I want to commend you for picking up on the suggestion of Congresswoman Furse in terms of this training idea. I think it is a good one.

In fact, not only is it a good one in this context, but we have actually seen it work in a similar program.

I have authored legislation that, in limited circumstances, allows the Federal Government to let people on unemployment pool their money for the purpose of setting up small microbusinesses, and in the areas where it is done, a part of the training of helping those people in terms of getting their business plan, getting their paperwork together so that they can make a justification that they can run an ongoing business has been very helpful, and, I think, picking up on the suggestion of Congresswoman Furse, it is a good one, and we will ask some more about that in a moment.

Let us go now to Mr. Burford.

TESTIMONY OF M.J. "MORRY" BURFORD, CHAIRMAN AND CEO, FIRST SECURITY BANK, AND CHAIRMAN, OREGON BANKERS ASSOCIATION

Mr. BURFORD. Congressman Wyden and Congresswoman Furse, my name is Morry Burford. I am chairman and chief executive officer of First Security Bank of Oregon, chairman of the Oregon Bankers Association, and a board member of the Federal Home Loan Bank of Seattle.

First Security Bank of Oregon is a subsidiary of First Security Corp. of Salt Lake City, Utah. In Oregon, we have 11 offices and $300 million in assets.

I am very appreciative for this opportunity to discuss what is unquestionably the number one issue of banks and bankers in Oregon and across America and that is our excessive regulatory burden.

Last year, the Oregon Bankers Association polled our membership, conducted personal interviews, and discussed regulatory burden at OBA committee sessions. I was surprised at the outburst of emotion that accompanied the dialogue.

Please understand that nothing has ever evoked the level of emotion among our bankers like the current regulatory environment that we live in today.

Bankers are angry that they cannot compete in the financial marketplace. We are angry because we can no longer take care of our customers in an efficient, professional manner.

We are angry because of the overreaction of Congress and regulators alike for the savings and loan debacle. We continue to be painted by the same brush and very unfairly.

Bankers are frustrated because it seems that no one is listening, and no one really cares, and these kind of sessions, I think, are great. We are listening to both sides, the businessmen, small businessmen, and the bankers, and what those problems are.

I personally know bankers who have left the industry just because of regulation, just gotten away from all the red tape.

Last year, First Security Corp. of Oregon bought a bank in Willamette Valley, a $30-million bank headquartered in Dallas, and the reason that owners, the senior management, who owned 58 percent of the bank, the other major stockholders, and the board of directors—the reason they wanted to sell was just because of the excessive regulatory burden.

It had become impossible for them to adhere to all the regulations without dramatically increasing their staff and, therefore, lowering their profitability.

You have a copy of my testimony. I am talking today really about residential real estate and commercial real estate, and how that affects the small businessman and those loans.

I brought with me today some loan files. That is a loan that was made in 1978, residential real estate. These are three piles, one being the conventional residential mortgage loan, and the other three, which are the same. Those are an FHA and a VA residential mortgage loan.

So, you can see, really, that speaks for itself. You do not need to discuss that.

The other thing I brought are just forms that are necessary to be filled out.

In this folder are the forms that an FHA builder has to fill out, the instructions and the forms. That is just to build a house, for the builder to fill out, not counting what the customer has to fill out.

I think how this relates to small businesses. When Congressman Kopetski met with First Security Bank employees a few weeks ago, I had a customer meet with him. This customer is a developer. He has all of his excess cash out now to small builders.

He charges them 12½ percent, 2 points, and they go to him because it is much simpler and faster to get a loan from him than it is to get a loan from us.

A lot of those same builders we would be happy to finance. We would charge them 8⅞ and 1 point. He is getting 12½ and 2, just because they can go to him. They do not have to get appraisals, and they do not have to wait four to 6 to 8 weeks for us to complete the paperwork.

So, it really is affecting them dramatically. He is making a lot of money, but it hurts the small businessman.

I think the difficulty that small business owners are experiencing in borrowing on their real estate—a lot of it is the overreaction to real estate problems that banks and savings and loans experienced in Oregon 10 years ago and certainly are still experiencing in other parts of the country today.

Regulators are much more critical today than they have ever been, quicker to classify a loan, which requires a bank to increase

their loan-loss reserve, and Congressman Wyden, you mentioned is that profitable business to us?

It is until they classify it. We put in a 1-percent loan-loss reserve when we make a loan.

Depending upon what the classification is, it can go anywhere from a 10-percent loan-loss reserve to a 50-percent loan-loss reserve, which obviously has dramatic impact on our bottom line.

If it is a $100,000 loan and you are charging them 8 percent, you have to put 10 percent in loan-loss reserves, and obviously that is not real profitable to us.

Another thing that is happening, I think, in banking today is that we are getting a little tougher on underwriting, and I think that is a safety and soundness issue, and I think, in some cases, it is certainly warranted.

I think our underwriting standards have gotten tougher. Cash payments are always required now. A few years ago, you could do a land-development loan with no cash down. That is not the way it is today.

Debt services ratios are higher on income property.

Another problem that is going to become a serious problem in the State of Oregon is the OPERS fund. We sold OPERS $165 million in loans. That was 530-some loans for an average loan balance of about $305,000. That program has been shut down.

OPERS no longer will lend money on Oregon real estate. Apparently, they would rather lend it in London, where they lost $25 million, or New York, where they lost another $10 million, I think.

At any rate, that is going to have a dramatic impact on small business owners in Oregon trying to borrow on real estate.

In addition, I think the lenders and borrowers have got to concern themselves not only with the bank regulations but with ADA regulations, environmental regulations, earthquake regulations, wetlands regulations, spotted owl regulations, and on and on.

To give you an example of regulations and the cost, I have a compliance officer, and that really is the only thing he does, is see that we try to obey the law.

I had him weigh our CRA file yesterday. He thought I was crazy, but I said there is a reason for it, weigh it; 76 pounds of documentation just in our CRA file. I was amazed myself. I knew it was big, but I did not think it was that big.

Anyway, in closing, I would like to make a few general comments.

I was an auditor for 7 of my 30-plus years in banking. So, I do understand the need for safety and soundness.

A few years ago, any banker would have been extremely upset about being criticized for breaking the law in the bank. Today, we are breaking the laws every day. It is impossible not to.

The regulations are too numerous, complex, and being added and changed so rapidly that management cannot keep abreast of them.

I think it is a sad statement. I think that is really a sad statement. It is impossible to go along.

We are really not criminals. We are an honest community of people, and we have been serving the business community and our customer base for a long time.

In summary, I want to reiterate that I support what has been implemented to assure real safety and soundness of the institution and meaningful consumer disclosures. The key words here, I think, are "real" and "meaningful."

Thank you for the opportunity. I would be happy to respond to any questions.

Chairman WYDEN. Thank you, Mr. Burford. We know of your willingness to work with Congress on the basis of past visits, and we appreciate it.

We welcome Mr. Humphreys from the other corner of the State and Juniper Bank in Madras.

TESTIMONY OF WILLIAM V. "BILL" HUMPHREYS, PRESIDENT AND CEO, JUNIPER BANKING CO.

Mr. HUMPHREYS. Thank you. Not exactly from the corner of the State. We are right at central Oregon, Redmond and Madras. Once again, I thank you both for allowing my testimony.

My name is Bill Humphreys, and I am the president and CEO of Juniper Banking Co., which is a small community bank, as I said, located in two small communities in central Oregon, with a total staff of 22, officers number six, and total assets of $26 million, about $20 million in loans, and we specialize in commercial loans to small- and medium-size businesses.

I wanted to share with you just two things and to try to bring this down to the level of the smaller community bank.

At our bank, we estimate the cost of compliance to be about $30,000 a year. That really equals about 25 percent of one key officer at each branch, their time.

What do they have to do? They have to keep up with a steady stream of paperwork. They have to educate the balance of the staff by sharing all that they know with them. They do internal auditing, and we respond pretty extensively to external auditing.

All banks are typically audited twice a year by different regulators.

We send two people, at least, to compliance seminars annually, and we also have a communication and training program for the board, because they are lay-people, and they need to know what is going on in the way of regulation.

What I really want to talk about, though, is not how expensive it is for us. I want to talk about how this burden impacts on our customers. It is impacting them, and I think it is impeding economic productivity in our area.

To do that, I would like to share two examples that are factual examples. In fact, I acted as the loan officer in both examples.

In the first example, a customer, who is a farm implement dealer, came to us and requested refinancing of a building previously purchased on contract 60 months earlier. The original purchase price in this case was $325,000. The balance needed to finance was $150,000.

The tax-assessed valuation on this property was $350,000, leaving a loan value of 42 percent on that transaction, and the customer applied for an SBA 7(a) loan guarantee.

Listing costs and requirements for this loan: The appraisal, of course, because it is over $100,000, is required by FIRREA, and we get good service in central Oregon. That appraisal only took 25 days—I mean 45 days, and $2,500 was the cost.

Then an SBA presentation package really needs to be prepared, not just for SBA but for the bank.

A presentation needs to be prepared outlining all the financial management stuff, goals, and the business plan, and I have brought with me today a copy of a typical SBA presentation package. In this particular case, that one cost $3,100.

During the appraisal, the appraiser pointed out the need for a possible environmental assessment, because there could possibly have been contamination on the property at some point in time, and so, we needed to have that done.

That report is done by a licensed and approved environmental engineer, and that took an additional 45 days, at the cost of $2,150.

By the way, to escape any kind of liability, the appraisers are now asking, in every case, for an environmental assessment.

The SBA charges a 2-percent loan-guarantee fee, $3,000.

Of course, we have a title insurance policy, and that is prudent on all real estate loans. However, if we were not to have it, we would certainly be classified as a substandard loan by both of two regulatory agencies. The cost of that is $1,050.

Total noninterest charges at closing on this loan transaction were $11,800 for this borrower. The transaction took us about 90 days to complete.

In this particular transaction, the bank did not charge a loan fee, and we also wrote a loan that is well below market rates. The SBA terminal rate is prime plus 2¾. So, you can see that we were the customer advocate in this case.

The second case is a situation where two orthodontists want to build a new medical clinic, and they need to acquire land to build a building on. Here are the details.

The land origination cost was $235,000. The downpayment they made in cash was $100,000, and they wanted to finance $135,000, and the building construction cost $300,000.

In this case, though, they were not ready to start construction of the building. They needed, however, because of certain circumstances, to acquire the land first and then put together the plans to build the building.

So, really, we had to make two loans. You go through the process twice, with all the costs twice.

The appraisal, $1,500; title insurance policy. In this case, as a direct bank loan, we charged a loan fee of 1 percent.

Environmental assessment was indicated to be needed. This was a large field of sagebrush and juniper, and no one could imagine that there might have been someone dumping out there, but that needs to be tested anyway.

The county requires engineers draft some plans with stamps from both architect and engineer. That was $3,500 additional.

That was really for the first loan, to acquire the land, and then we made a second loan to build the building and went through all of those costs once again. So, this customer paid a total of $20,100 for a new medical clinic building at 80 percent loan to value.

Also, I might state that the building originally was designed to be a two-story building, but because of the Americans With Disabilities Act, they changed the design, and it ended up to cost more, because the larger dimension on a single-level building increased the cost of construction on that particular piece of property, and I do not have a figure for you there.

So, $20,100 in this particular case.

I have also got an additional sheet of paper that has some facts. I will not go over all of these, but it is just an outline of the typical $200,000 loan, the costs, and the time to complete.

The average cost to make a $200,000 SBA 7(a) guaranteed loan is around $12,875, our estimate. It takes about 122 days.

One advantage to getting an SBA loan is to get that prime plus 2¾ percent fixed interest rate for the term of the loan. There are really no other obvious advantages.

Thank you.

Chairman WYDEN. Mr. Humphreys, thank you.

We will have a chance—at least, I will—in another part of my Congressional life, I sit on the Energy and Commerce Committee, where we have jurisdiction over the principle environmental programs, Superfund and RCRA. We will be anxious to work with you on single-lender liability issues.

Mr. Brawner and others, I think you have made a compelling case that we need some reforms. They are up for reauthorization this year.

I have some questions, but let me first recognize my colleague.

Ms. FURSE. Well, I had actually two comments, really.

Mr. Brawner, your list of recommendations, I think, is incredibly helpful to me. I am on a high learning curve at this moment. So, that is going to be very useful to me, and I am certainly going to go through those and see what we can do to see how that possibly can be brought in.

I have an open-ended question. How can we deal with public perception? As you know, people are lumping the savings and loan crisis, and they are saying regulation must be good. How do we deal with that, in your view?

Mr. BRAWNER. Congresswoman Furse, I believe a large part of it is we have to do the dealing; we have to talk to the public about these things in American banking. Of all banks in America, 96 percent today are profitable.

Not a single dime of the $30 billion that was set aside as a line of credit for the FDIC fund has been used, and we do not expect that to be used.

I think the Congress, the media, and the banking industry have come through some very trying times. I think we are out of those times. We ought never to forget those times.

When I was brought up as a brand-new loan officer, I was told you cannot make a bad real-estate loan. Now we know that we can, and so, I do not think we will be doing that again.

I think we have a responsibility. I think the Congress has a responsibility. I think the committee that we are fortunate enough to have you represent us on has an obligation to make sure that we deal with facts and not fiction.

There are those who are still writing books about the December surprise, which turned out to be a December dud. Instead of 1,000 banks, 6 banks failed when the new capital requirements went into place, but we have a responsibility to do that.

You mentioned, in the previous panel, education of small business people. You will hear later this morning about a program that we have been participating in, and we think education of our borrowers and education of our loan people is an ongoing process.

We certainly appreciate this opportunity to set the record straight. Oregon banks, particularly, rank first, second, or third in safety and soundness of all banks in the country, and maybe we do not tell enough people.

Ms. Furse. Thank you.

Mr. Winnowski. Just an additional comment along that line; I think one of the things that can best portray the banks' position as far as small business loans is concerned is to look at testimonials from the people we serve and who are served well.

We have a lot of small business customers. There is not a void in the way we look at things.

We have two officers in the audience here whom I referred to before who are community business lenders.

All they do every day is to deal with these clients, and some we advise, some we directly lend to, and some we advise to go elsewhere, but the ones whom we have as customers, I think would be a good testimonial as to what banks are doing to serve small businesses and perhaps learn from them what they did in order to get their loan from their bank.

Mr. Burford. Just a real brief comment on that, Congresswoman; I think that there was not enough looking done by Congress to really take a look at why the savings and loan fiasco took place. It was an educational process they needed to go through, and they did not.

I understand you have a lot of educational issues there, but they did not take the time to go through and figure out why the savings and loan fiasco took place. There are some very logical reasons for it. There really are.

In 10 minutes, I could explain to you most of them, but Congress did not take the time to do that. It was a knee-jerk reaction.

They said we cannot let this happen again. It is costing us billions and billions of dollars, and we have got to regulate the banks; we have got to do that.

Mr. Humphreys. I think public perception needs to be worked on. I agree with what Frank said. We need some image-building and a good deal of positive marketing, but down in the trenches, I think education is really the key.

A lot of small business people come to me, and I am one of the CEO's in Oregon who also acts as a loan officer for my bank, and I get to talk to these people on a direct basis.

When they come and sit down, and they talk about financing for their business, the element that is typically missing is the financial-management aspect of their business.

We look at business management as a three-legged stool, with the key elements of management being marketing, the production, and the financial-management aspects.

The thing that they typically do not bring to the table is a good understanding of how the business works financially, and that kills an awful lot of deals.

When we try to educate our customers and then maintain that education after the business has started, we are subject to liability issues.

So, we are required, because of the fear of liability, to back off. So, we need help.

We need help at the SBA. Community colleges are trying to do that job. I know some chambers are trying to do that job, but we need a lot more education.

Ms. FURSE. Thank you.

Chairman WYDEN. Well, a couple of questions for all of you, and you have been very helpful. Suffice it to say I know of your sincerity and the fact that your banks are willing to be part of supporting the Little League teams and community services and that you wish to be good corporate citizens, and I think that we know what needs to be done. We have to increase this lending.

Clearly, there are some obvious regulatory changes that are needed, but I think really the question is how to get it done. Let me ask you first to pick up on one of the questions my colleague had asked.

Are there some alternatives to classic deregulation? The first thing, of course, citizens think about when they hear about deregulation is, as my colleague has said, about the savings and loan situation.

In the environmental area, there has been considerable progress that has been made in this regard.

You look, for example, at the Clean Air Act, where our committee was very involved in the last session, and clearly we have moved in that statute and in environmental statutes to a much more market approach, an approach with real incentives or, as Mr. Brawner has talked about, the banks and institutions that do comply with the rules.

Are there some ways in which we can take some of the incentive concepts that we have seen begin to work in the last few years in the environmental area and apply those in the financial area so that we can accomplish the objective that you are talking about, which is to get rid of some of these regulations, without just the classic deregulation, where you just throw everything out the window and the person you ought to be watching gets treated in the same way as the person who has shown a good track record?

Mr. Brawner.

Mr. BRAWNER. I believe that well-run banks, banks that are rated one or two, ought to be given the latitude to venture forth perhaps accepting noninsured deposits, perhaps engaging in activities heretofore thought not to be desirable for banks to do but allow them the opportunity to be competitive with some activities, serving small businesses. Why can't a bank become an investor in a small business?

Where does it say that we in America have to treat our banks differently than they are treated in England or Japan? Why can't we accept noninsured deposits and disclose to the public that this window accepts noninsured deposits?

I think there is a lot that could be done, giving well-run banks the opportunity to venture forth, creating the incentive for well-run banks to do more to serve their customers. I think there are some creative ways to make it happen.

Chairman WYDEN. Each of you will not be required to answer, but if you wish to answer, we will be interested in your thoughts.

Mr. WINNOWSKI. I think that in terms of appeasing and appealing to all groups, both the bank side and the small business side, I think that the one suggestion that we came out with concerning this specific exemption for customers who exhibit financial strength in order to be relieved of some of these burdens would appear to the public and to that small business that you are actually giving them something back for having taken this deregulation away, and you have not affected the safety and soundness of the institution.

So, from the customer's standpoint, I do not think you would get any adverse reaction from people for deregulation if they understand that they have taken a step forward.

Mr. BURFORD. I think, too, Congressman, that deregulation is an interesting term, but as Frank pointed out, we have had 44 major pieces of regulation in the last 2 or 3 years, and they are still coming.

It is like a machine back there. I do not even know where they are all coming from.

We are not asking you to deregulate banks, most certainly. I do not think that anyone sitting at this table would probably say that we should have absolutely no regulation.

What we want is a reduced level of regulation that does not affect the safety and soundness issues and is meaningful for the consumer.

There is a case for consumer protection, and very little of it is for safety and soundness. I do not think there has ever been a bank in the country that went broke making home loans. So, this is not a safety and soundness issue.

This is part disclosure, part whatever, so, I think some reasonableness and not calling it deregulating the banks would help the issue.

Mr. HUMPHREYS. I would like to answer, too.

To me, classic deregulation is adding another regulation or adding another program to help to deregulate, and I am afraid that might happen in this case.

What I would like to see done is work on our existing programs, so that they can be more effective. Let us take the SBA, for example. I am a real SBA loan advocate. We like SBA loans. We use the SBA 7(a) guarantee program a lot.

A lot of people probably do not know that in the Portland office of the SBA, where they originate 7(a) guarantees for all of Oregon and Southwest Washington, there are only two loan origination officers and staff of four for loan origination.

I have two loans pending right now at the SBA office that I am told we just need to wait until that stack of 30 to 40 pending loan transactions falls down to where mine is.

So, I think we need to work on some of the programs that we already have. They are very effective programs. Staffing has been

cut back so badly at the SBA. They are very good people, though. They do an excellent job.

They are just ineffective because of the staffing cutbacks.

Chairman WYDEN. Let me ask you now to hang onto that account in great detail, because as I work on this SBA overhaul bill you may have heard me mention, the big objective is going to be to get some of those folks out of Washington, DC, and get them out around the country where we are hearing these kinds of examples of paperwork backing up and not having enough of the loan assistance officers and the like, and I would like to be able to have that account, and do not let it fly from your memory, because it would be very helpful and very much in line with this SBA overhaul bill that I have been hatching.

Mr. Brawner.

Mr. BRAWNER. Could I just add something?

Mr. Chairman, this study finds in its findings that there is no process in place to bring about the repeal of obsolescence regulations that were passed 15 years ago. There is no review.

There is a statement in the report that I think is well for this panel to wind up on. It is five criteria for bank regulations brought to these people by community bankers:

Is the regulation economically feasible and practical?

Are there existing regulations that suffice?

Does the regulation allow bankers to be bankers?

Is there a sunset provision in the regulation?

Will American society be better off?

Now, I think, if we could ask those five questions about the burden that we have now, we would be able to operate and compete.

Chairman WYDEN. I am going to have to ask you one other question before we let you take off.

On this point that you were making, I think that there is considerable merit to the idea of automatic review of regulations after a period of time.

Of this working group that we have been discussing, I would like to have you look at the other matter that I talked about in terms of are there some market incentive approaches that might get us out of this classic regulate-versus-deregulate kind of debate which we all see as a bit mindless, and second, I would be very interested in your thoughts on what might constitute a reasonable period for triggering automatic review of regulations? Let me also ask that you pursue the suggestions that Congresswoman Furse has made today about the training, which I think makes sense, and her comment about the high-technology area, as well, where I think our whole delegation shows considerable interest.

Let me ask you one other one that I just talked with Mr. Winnowski a bit about yesterday.

When Congresspeople work on all of these things—we have got the 32 items in the regulatory burden relief legislative proposal, and the figures are $10.7 billion for unnecessary regulations—what our constituents are going to ask is what is it going to mean for them in terms of benefits, as it relates to lower costs, more loans, things that, in effect, say OK, after everybody labored hard to work

on these, and we do not question for a moment that many of these are valid.

After all of this is pursued and many of them accomplished, what comes out at the other end, in your judgment, in terms of lower costs for people, more loans and the like?

I am of the view that, if we are to really make this partnership work in this Congress—and we have discussed it with some of the President-elect's transition people—it is going to be necessary to quantify this.

I mean it is going to be necessary to really show that, with these kinds of changes in the regulatory climate, out at the other end is going to come such-and-such in the way of more additional loans, such-and-such in the way of reduced consumer costs.

What can you contribute on that point this morning? I recognize that some of this will take some further analysis and some work.

Mr. Winnowski.

Mr. WINNOWSKI. Let me just tie that to another subject that was brought up earlier, and that is the SBA.

We are an advocate, also. If I could just leave you with that one impression, it would be, I think, well, that we are an advocate, also, of the SBA route in terms of allowing for more credit to be available.

In fact, we, in 1991, were the number one lender in the State of Oregon on SBA loans and, in 1992, the number two lender.

The system works. It may need some modification, however, as Bill has pointed out.

If I could make the recommendation to you to take a look at just the SBA process alone, to try to make it something more manageable. You have an agency, you have a defined set of paperwork, you have defined guidelines, and you know exactly what banks are certified lenders and preferred lenders. All of that is quite public. That is controllable.

Take that and try to define whether or not you can cut down on a lot of the red tape.

Make it a better, more efficient type of operation, and I will say to you, whether it is that route or taking 30 of the 32 or 35 issues on that piece of paper, you now have a banking industry that is lined up, saying please help us, please help us to get rid of all of this.

If they see action on that end, I think, automatically, they will respond, not to the extent of doing 250 more loans than XYZ bank, more than they were a year ago, but you will see, in the overall, we will try—I think I can speak on behalf of the Oregon Bankers Association as well as the industry—to look at ourselves, to examine ourselves from time to time and make sure we have responded. I think you will see it.

Mr. BRAWNER. Mr. Chairman, no banker enjoys investing in U.S. Treasuries. Every banker I know enjoys making loans. That is the satisfaction, creating jobs.

I have bankers call and tell me I have done this and this and this, and that company now employs 50 people, but I cannot tell anybody about it, because it is confidential, but I am proud of that. I have never had a banker call me and say I just bought another bond.

I think the motivation of this industry is to do what you want us to do, make loans, but when you have examiners with zero-based tolerance, which is found in this study—so the message coming from Congress is, wait a minute, we did not mean zero-based tolerance; we mean that there are rules, but they are going to be meaningful rules, not unbelievable rules; get back to the business of running a bank and doing what bankers can do.

So, I think the incentive is there. The illustration of the difference in reserves between investing in Treasuries and investing in small business loans—that can be addressed.

A lot of this can be addressed very simply, without throwing the baby out with the bath, just reducing the redundancy.

Real estate lending is defined four different ways in the same Federal statute. What rule, what definition do you want us to play with?

We have already gone overtime, and I hope not outworn our welcome, but I can tell you, we can go on and on and talk to you about incentives that it would not take a whole lot to get us—at the Clinton economic conference, the figure—just let us make 4 percent more loans and that is $86 billion back out there financing America's business.

Chairman WYDEN. I want you to know that I know of your interest in working with Congresswoman Furse and me and the kind of commitment that you all have made to Oregon communities, but you should also know that the question that I have asked is going to be asked in many other forums by people who are going to say banks in our community might not be willing to make additional loans even if they do get regulatory relief; maybe they are going to just go out and boost their profits.

I think, to really make this partnership all that it can be in terms of Congressional legislation, in particular, and allowing people, like Congresswoman Furse, who are going to be in those Banking markups trying to wrestle with a very complicated set of proposals, we are going to have to work together in order to try to quantify how, as we make some of these sensible changes that are being discussed in the regulatory area, that people will really see, at the other end of the line, reduced costs that they can understand in their lives.

Yesterday, Mr. Winnowski took me through a nightmare for what amounted to a $99 fee, and I think if we can take some of those rules and show that, at the other end of the line, we have a prospect for lowering the charges and generating more loans, we give people, like Congresswoman Furse, who are going to be in those Banking markups, and myself, as we work on the SBA changes, some fresh ammunition to work with. Unless you all have anything further, we can excuse you now.

Thank you for coming.

Our next panel: Sandra Suran; Carl Flipper; and Professor Harmon. The issue is emerging enterprise plans.

We welcome all of you. We know of the good work that you have done and have had a number of occasions, both of us, to work with all of you.

It is the practice of the subcommittee to swear all the witnesses. Do any of you have any objection to being sworn?

Please rise and raise your right hand.

[Witnesses sworn.]

Chairman WYDEN. If you could, try to stick to around 5 minutes or so. We will have some questions then.

Ms. Suran.

TESTIMONY OF SANDRA SURAN, PRESIDENT, THE SURAN GROUP

Ms. SURAN. Thank you.

Thank you, Congresswoman Furse and Congressman Wyden, for letting me have the opportunity to address you. I have been interested in the issue of access to capital for small businesses for probably over 20 years.

I am currently president of the Suran Group, which is a consulting firm. I was the first small business advocate for the State of Oregon in a loan executive position.

I also have been on the Federal Reserve Bank Board at the Portland branch and served as 12th Federal Reserve District's chairman of the Advisory Council on Small Business.

So, the remarks I would like to make are really from the perspective both of interest in small business, as well as a small interest and knowledge of the banking community and their issues and problems. I have been watching from that perspective.

Probably over the last 10 years, what I have seen is a changing attitude toward small business in the banking community and the Federal Government, and regulations and I have been very concerned over that time, because what I have seen is a reaction to economic issues, and that is what I would like to speak to.

In reacting to economic issues, in particular, I have seen banks in a free-market economy reacting to increased competition and increased challenges to their viability with free-market-type responses. That is, mergers, changing their ways of doing business, and changing their responses to risk.

At the same time that they were taking basically free-market responses to the economy and to increasing competition, we saw the Government jump in and attempt to do the same thing through regulation and mandating requirements.

So, we had both free-market responses as well as the reaction through regulation, and what resulted, I believe, was overkill that affected basically the most important growing part of the American economy and, in particular, Oregon's economy.

Just to give you a little bit for the record, approximately 80 percent of all businesses in Oregon have sales of less than $1 million a year. So, in that group, we are not only talking about small business, we are talking about very small business.

That represents 80 percent of the businesses in Oregon. That also represents in Oregon approximately 90,000 companies that do less than $1 million a year.

Approximately 85 percent of those companies have also less than 20 employees, but recent statistics have shown that segment, with less than 20 employees, which is again very small businesses, provided all of the net new jobs in Oregon.

This small business segment, therefore, is critical to the growth and development of Oregon. So, contrast that importance of the

small business sector with the banking trends nationally in Oregon.

First, to remain healthy—and, of course, for this economy to survive, we need healthy banks—banks must reduce their risk of loan losses.

Recent Federal regulations have made that risk assessment—have made it a technical stringent exercise and have removed the judgment component, which is critical in assessing small businesses.

Small businesses simply do not fit any standard norms that more sophisticated, larger businesses do, and so, falling back onto the stringent technical exercise has impacted them negatively.

Second, to be profitable, banks must maximize their return, and that means minimizing the processing and administrative costs per loan and also increasing the productivity, and that means giving larger and larger portfolios to loan officers in order to increase their productivity, again in order to respond to the need for them to be profitable in an increasingly competitive market, but both of these profit-oriented directions work against small business loans, which typically require more processing time and do not fit well into standardized, ratio-oriented assessments and administrative programs.

They simply take a lot of time and judgment, and, of course, here part of the answer is through education, education of the small businesses, and we have some excellent programs, including the SBDC's and the SBA's, which can assist in increasing that educational ability base which previous speakers talked about.

Then, the alternative, if banks are not able to, because of reducing risk and the need to increase their profitability, loan in large masses to this very large segment of companies that are very small, then the alternative could be the Government. But government in Oregon, for example, simply does not have the funds to finance the tens of thousands of small businesses needing outside financing for growth and who do not fit under these norms.

So, Government does not have the funds to do that if the private sector cannot.

Additionally, given Government as it currently operates, the paperwork and the bureaucratic processes and bureaucratic requirements which are demanded in order to get these loans is extremely costly, both in the frustration it causes, in the lost time it causes, and in the diminished flexibility for the lucky few businesses that qualify, and as an example of that, in talking to the small businesses around the State that have received some of these Government loans, even the ones who had received the loans stated that they would not do it again due to the cost of time and frustration.

Some banks have recently set up funds outside their normal banking process to assist them in being more responsive to businesses and in being more responsive to their CRA responsibilities in the area of small businesses, but the funds available through these new programs that some of the banks have set aside simply are not adequate, again, to finance those tens of thousands of smaller businesses that cannot meet the technical requirements and are not able to get those loans.

So, the answer, then—and I would like to throw out four suggestions—is a combination of banking and the Government, which would, first, use Governmental funds not to make loans, since the funds that they have available simply are not adequate, but to use those funds to reduce the risk of loss for the banks that make those loans and to compensate the banks for some of the increased administrative costs of what it takes to make those loans.

The second would be to let the banks administer the loan programs.

The third would be to charge the banks with setting up educational programs for their loan officers to train them in assessment of small business financial potential and strength, to return some of the judgment to the analysis and not just use the standard ratios, since those do not work for the growing or for the very small businesses.

Fourth, as part of those programs that might be through the Federal or State agencies, give the banks results-oriented goals, rather than stringent regulations that are precise and relate to technical points of each loan.

Give them results-oriented goals, minimize the detailed hoops that they need to jump through, and the detailed paperwork usually associated with Government financing.

Thanks.

Chairman WYDEN. Very helpful.

Let us go to Mr. Flipper.

TESTIMONY OF CARL FLIPPER, EXECUTIVE DIRECTOR, OREGON ENTERPRISE FORUM

Mr. FLIPPER. Good morning, Congresswoman and Congressman.

My name is Carl Flipper. I serve as executive director of the Oregon Enterprise Forum. OEF is a chapter of the Massachusetts Institute of Technology Enterprise Forum Network, an entrepreneurial clinic that provides pro bono services to emerging small companies.

While the emphasis of the MIT Enterprise Forum historically has been technology-driven and growth-stage businesses, the Oregon chapter works with a more diverse range of companies, providing assistance to conceptual and developmental stage all the way to mature businesses.

OEF is just over a year old and has provided services in both urban and rural Oregon and has already provided services to varying industrial segments; software, electronics, and energy, to name a few.

OEF is affiliated with the Portland Metropolitan Chamber of Commerce.

Central to the services provided by OEF is the private panel review which matches three qualified business experts—generally, one in financial, one in marketing, and one in management disciplines—also with matching industrial experience, who spend a total of 18 to 24 hours in reviewing the business plans and operations of a business and providing no-holds-barred opinions, recommendations, and advise on how the entrepreneur should proceed.

We call this the Dutch uncle approach in just giving the entrepreneur a comprehensive checkup and evaluation.

The focus of this hearing, as I understand it, is to discuss ways in which legislation, either its repeal or adoption, can affect the smooth and efficient flow of final resources, debt, and equity, to the small business.

There are many regulatory and tax policies, as we have heard already discussed here, that bear directly or indirectly on the issue of capital flows, and I am not prepared to advocate the adoption of or repeal of specific measures at this time.

However, it is our experience that the access to capital is influenced by the small business person's knowledge of, one, the type of capital that he or she needs—that always relates to the stage of the development of a business—and second, who the providers of those specific types of capital are and the criteria that they evaluate the worthiness of the investment or the loan.

To the inexperienced business person, that person frequently believes in what I call the Willie Sutton syndrome, that banks are the only source of capital, and I do not want to sit here and hold banks entirely responsible for financing small business development in this country.

To the experienced business person, uncertainty generally exists as to issues as to whether or not to pursue some long-term equity financing or IPO, and there are questions that even the experienced person has, and we will hear of the wide range of capital sources available to the small business or the emerging business during the overall stage of that business' development.

Still other companies, particularly the microenterprises, are denied access from traditional sources of capital, because their requests are too small.

I have heard that transaction costs are generally too prohibitive to make a $5,000 loan attractive to many of our financial institutions.

Some banks, in recognizing certain economies, will obviously rather write 1 $100,000, rather than to write 10 $10,000 loans simply because of the paperwork involved and the monitoring costs involved with servicing those loans.

Some small businesses are quite legitimately concerned about some discriminatory issues which affect some of our women-owned businesses and minority-owned businesses across the country.

Other entrepreneurs, quite frankly, are just not realistic about the sources of money or what their capital requirements are.

We heard at a hearing several months ago from a business that was seeking some debt capital. That business person was tapped out in terms of his assets that he could use to secure the indebtedness. Yet, he was not interested in any partnership relationship whatsoever.

He wanted no equity capital, yet could not support any debt issue.

So, we find many entrepreneurs are just not realistic about the sources of capital and what is actually required.

OEF believes that the multiplicity of sources and reliability information about the requirements of those sources can facilitate access to capital.

This is not to say, however, that additional sources are not needed or some of the regulatory conditions should not be lifted to promote that access.

We heard about microloan programs, circular loan programs, such as for Compagna and Bangladesh Bank. Many of those loan programs—and they are microscopic size, $1,000 or $2,000 loans—are administered by many CDC's across the country.

These kinds of programs might very well serve small and microenterprises across the country.

Chairman WYDEN. Well said, Mr. Flipper, and we thank you.

Professor Harmon.

TESTIMONY OF ROBERT HARMON, PH.D., SCHOOL OF BUSINESS, PORTLAND STATE UNIVERSITY

Dr. HARMON. Congresswoman Furse, Congressman Wyden, thank you very much for inviting me to testify today.

What I am about to tell you today is the story of the ongoing transformation within the School of Business and Portland State.

About 2 years ago, we realized that the types of people who we were training were primarily going into middle-management jobs, and if you have been looking at the layoffs with the Fortune 500 companies, and so forth, nationally, we were finding that many of our graduates were being trained for jobs that did not exist and really were not likely to exist.

In Oregon, Fortune 500 companies or Fortune 1,000 companies are in very, very short supply.

We initiated a survey at that point in time to really take a good look at where many of our graduates were ending up, those who were staying in the State, and many of them were ending up in what we call emerging enterprise or emerging growth small businesses.

Now, this has a problem of expectations on the part of many of our graduates, in that many of our MBA students wanted to come out and make $50,000 a year in a nice secure job, that type of thing.

So, what we basically have been looking at is changing our curriculum to recognize that, certainly with small business, there is a risk but that there is certainly a lot of emphasis on the reward that can come from helping these types of firms.

Personally, I talked to about three dozen companies that would qualify as these emerging enterprises, and I asked them, why is it that you always hear that there is no training available, there is not the type of expertise available when it is at the university?

They really never saw Portland State as being a resource to them. They thought the graduates coming out very highly trained might be too expensive, and would not want to work for them anyway.

The faculty working as consultants really were not a resource to them, because it was too expensive, that type of thing.

So, we put our heads together at the university and came up with a proposal that is in the final stages of completion right now, and what we are trying to do with it—I will run through some of the things—is basically provide a resource base that would allow

emerging enterprises—and these are companies that are beyond the initial capital stage.

They have gone through startup, and they are up and running, but they are really starting to run into problems in management, capital formation, systems, and that type of thing.

One of the big areas that we found in terms of needs, in particular, in convincing bankers that they should give a loan to a company is not only the fact that a business plan exists, because many companies do have a business plan, but it is actually the quality of the plan.

Do they really understand the needs of the marketplace? Do they know how to identify those types of opportunities?

At Portland State, in the business school, we have a very good capability to help firms do exactly that, also developing plans and strategies once they have identified those markets, and developing new production techniques.

Portland State has been a leader in total quality management education, converted over to that about 2 years ago.

We also have excellent expertise in finance, human resources, and information systems, and last but not least, in the evaluation and assessment, feedback and control, accounting.

We have a very excellent accounting group there, and also, we are embarking on programs on how to measure customer satisfaction, which I think is really the purpose of much of this.

In order to do this, we have proposed the Emerging Enterprise Center, and I wanted to go through just briefly the objectives of the center.

Chairman WYDEN. At this time, I am going to have to try to keep everybody to 5 minutes. We have a whole lot more witnesses, and we will put all your comments into the record.

Dr. HARMON. OK.

Chairman WYDEN. Would you like to add anything else on the center, perhaps, one or two highlights?

Dr. HARMON. Yes.

I think one of the areas that we are really putting some emphasis in is minority- and women-owned business and also family-owned business. Many of the small businesses in Oregon tend to be family-owned, 76 percent, and I think that it is an emphasis that really has not shown up in any of the traditional education in the past, and I think that you are going to see more and more of it.

Chairman WYDEN. I thank you. I think you are aware that Dr. Ramilie and I talked about the emerging enterprise effort some time ago, and when she decides that she wants a program like this, bulldozers begin to commence shoveling.

I want to commend you all for the way you have moved so fast, and we have enjoyed pursuing it with you. We are going to work very closely with you on it.

Let us go to questions and begin with Congresswoman Furse.

Ms. FURSE. Well, a comment, really. It is very exciting for me to see the academic, public, and private partnerships that have come out, and that I can see emerging out of this hearing, and I will certainly pursue that.

I am very interested in the enterprise zone and obviously very interested in the whole idea of women- and minority-owned busi-

nesses. I think that is an emerging field that I will certainly put a lot of attention to. Thank you for your information, and I will study that.

Thank you very much for your presentations.

Chairman WYDEN. Only one quick question, and I think we are all beginning to ask it more.

Today, it is possible for small business to look at a variety of places: The State, the SBA, the chamber of commerce, and small business development centers. Oregon State has a program.

I think what we are starting to see is that a lot of entrepreneurs are asking, with all of this, where exactly do I go to turn to do this quickly, to get into the system, to find out what is available to me, and to make this happen with real speed?

Is it your sense that what is needed is some way to create a central clearinghouse for this kind of information and assistance, so that small business people who are working their heads off from morning to night and do not have much time can get it and get it fast?

Ms. Suran.

Ms. SURAN. That would be a real benefit to small businesses, and, in fact, when we did a study around the State, small business' greatest need is a way of accessing the resources that are already there. There is so much, as you have described, Congressman Wyden.

There is too much for them to be able to easily research, and having a central resource that would assist them in targeting the places to go to get information would be a great benefit.

Chairman WYDEN. Well, let us also ask our working group, which has a good four or five items in front of us, to also pursue this, because what you and others have said in the past has impressed on me how important it is. We will be looking forward to working with you in the days ahead. Thank you.

Our next panel is going to be Mr. Rich Brown, Bank of America; Ms. Karen Tolvstad, US Bank; Mr. Warren Townsend, Oregon Economic Development; Mr. Sandy Cutler of the Small Business Development Center; and Mr. Rey Ramsey, who heads our housing program and has done an outstanding job in many areas that we are concerned about.

If all of you will come forward, we are going to swear you in quickly. We welcome you. Are we missing anyone? Mr. Brown, of all people. All right. We may have to swear him when he comes. Do any of you have any objection to being sworn as a witness?

Please raise your right hand.

[Witnesses sworn.]

Chairman WYDEN. Why don't we begin with you, Ms. Tolvstad, if we could? I do need to ask all of you to stick to 5 minutes if you can.

Thank you for your patience. It has been a long morning, and you all have been more patient than anyone. So, please proceed.

TESTIMONY OF KAREN TOLVSTAD, VICE PRESIDENT AND COMMUNITY INVOLVEMENT MANAGER, U.S. BANK, PORTLAND

Ms. TOLVSTAD. Thank you.

I think part of our panel's responsibility today is not to let it end on a doom-and-gloom note, talking only about the barriers but about some of the initiatives that we have made here in Oregon in spite of those barriers.

I am here today representing not only U.S. Bank, the largest small business lender in the State, but also the Oregon Bankers Association, as the Chair of the Community Involvement Committee of that organization.

I would just like to say that Oregon banks are committed to meeting the needs of the community.

We have several aggressive initiatives that we have done, not because there is a law to make us do so but because it is good business and because it is good for our communities, and these are our communities, as well.

Some of how we are doing that with the regulatory barriers that we are under is through partnerships and finding creative ways of meeting the needs of small businesses, such as providing funds to CDC's that then loan those funds out, like the Oregon Association of Minority Entrepreneurs, a loan fund that is up to nearly $3 million from four banks contributing, and then they lend to minority-owned businesses.

Also, reaching out to unique Oregon industries, like the nearly 1,200 businesses in the secondary wood products industry.

We are getting ready to embark on a cooperative workshop to talk about how Oregon banks can meet their needs better.

Also, both in partnership with all of the banks, as well as the individual banks striking out independently, working smarter, listening to our communities, our bank goes around the State holding community forums, meeting the small business owners, asking them what they need from us in order to have us be more responsive.

Many of those things have resulted in new products and programs and how we are organized.

I think Mr. Winnowski referred to organizing ourselves and creating things like small business specialists.

Our bank has eight small business specialists throughout the State who specialize in meeting the needs of very small businesses and specialize in programs like Mr. Cutler will speak about and Mr. Townsend.

Also, creating responsive loan products, working within the regulatory environment to structure special products that can offer flexibility to real target markets.

U.S. Bank offers a small business credit line where borrowers can apply just once and access a credit line that they can tap into without jumping through all those hoops time and time again.

That product allows borrowers to borrow as little as $5,000, and again, what we are hearing a lot is the need to tap into very small amounts of funds in a way that is cost-effective; also, products like our own opportunity loan program that offers extended terms and some flexibility in underwriting for women- and minority-owned businesses, again reaching out with a very targeted product that the regulators will approve as well.

I think these examples are just to show you that we are poised and ready to meet the needs of the small businesses in our community.

With some more support and partnership with Government, I think there is no end to what we can do.

Thank you.

Chairman WYDEN. Very good.

Mr. Ramsey.

TESTIMONY OF REY RAMSEY, DIRECTOR, OREGON HOUSING AND COMMUNITY SERVICES DEPARTMENT

Mr. RAMSEY. Congressman Wyden and Congresswoman Elizabeth Furse, I am pleased to be here today. I will adhere to the 5-minute rule. That is not easy for me all the time, but I will do that.

I would like to talk a little bit about the interrelation between small business development and what I call healthy communities and the housing market that we have in this State, because, obviously, the interrelation between healthy businesses and communities are self-evident and undeniable.

I think we can all agree that small business needs access to capital, training, technical assistance, and regulatory relief.

You have heard a series of suggestions today put forward by Frank Brawner and others, and I would agree with most of what they had to say, but one point I would like to make is that we do need nontraditional means to make this happen, because, although things have gotten perhaps worse for small businesses in Oregon and in the country generally, things have never really been the way we would like them to be.

So, I am cautioning that, if we say let us go back to the good old days when there were fewer regulations, the job was not really necessarily getting done then, and we still have problems today, particularly in our cities and in our urban core, for women, minorities, and the disadvantaged.

Examples of nontraditional approaches, I think, would be using community development corporations. That is something that my department, the Oregon Housing and Community Services Department, has been involved in.

Karen Tolvstad mentioned a little bit about secondary wood products. What we have done is we have worked with a co-op in rural Oregon, in Roseburg, to form a secondary wood products co-op. That co-op is not going to be successful without access to capital.

What the State was able to do with public funds was to get that co-op started, and the advantage to that was that they could share costs, some of their initial startup costs, their joint marketing costs, et cetera.

I think that when we think of community development corporations, often, particularly in Oregon, we think about housing, but there is a lot in business development and economic development that can be done.

So, I would like to see more done with working with community development corporations and perhaps educating more lenders and other people, who may not be as sophisticated or as involved in it,

to get more involved in that, because I think there is a terrific future there.

There is also another community development corporation in Hood River that is getting involved in daycare centers and moving that as a kind of microbusiness. I think that there are things that we can do there as far as lending practices to those kinds of corporations.

In addition, another concern is the way we deliver our educational and technical assistance or lending. We have to do it in a user-friendly fashion.

We can have it in development centers or we could have it at universities, but, at the same time, we need organizations that are culturally sensitive to women, minorities, et cetera. So, the way we deliver those services, I believe, is important.

I would also like to say, though, working with the banks and the lenders in Oregon has been a terrific experience in the 2½ years that I have been director of the department and also, previous to that, working in the Economic Development Department at the State.

U.S. Bank, in particular, has lent an executive to my department at no cost to our agency to help us in designing some of our programs so that they would be user-friendly to the banks, because we cannot be successful in these programs without banks being involved.

So, the banks have stepped forward and have helped us out, and the partnership is great, and we appreciate it.

What I am calling for is making sure that we look at some of the nontraditional means of lending, like looking at co-ops and community development corporations and making sure that the cultural and ethnic sensitivity is there in the way we deliver these products and services, whether they be SBA or whether they are the lenders that we have.

Chairman WYDEN. Very helpful.

Mr. Townsend.

TESTIMONY OF WARREN TOWNSEND, CAPITAL ACCESS COORDINATOR, OREGON ECONOMIC DEVELOPMENT DEPARTMENT

Mr. TOWNSEND. Representatives Wyden and Furse, I am Warren Townsend. I have been working for the last few years with economic development for the State of Washington and now in the State of Oregon. I set up and manage programs.

To keep this on a high note, I would like to bring to your attention today the capital access program of the State of Oregon, one of the programs that I think is revolutionary in design and is not only successful but is accelerating its success.

The program was designed to promote lending by banks to small businesses that just miss the normal lending standards of most banks. In other words, there is a level of risk up here just above the normal standards.

This program permits the bank to step into that level of risk and make a loan to a small business. We call them the almost-bankable businesses or the almost-bankable loans.

The business gets a loan it would not otherwise have gotten, generally at a cost much lower than it would cost that business to go out and find the money elsewhere, even from relatives. They can be the worst.

How is it done? It is a form of loan portfolio insurance. I will not get into the details, but it is a funded loss reserve against which a bank may draw if a loan goes bad.

Barriers to the program—I was asked to comment on those, and there really are not any great barriers. There are perhaps two things to bring up.

One, the banks themselves: Perhaps with education we will get more banks in the program, and I will mention something on that in a moment, but banks have to learn to use the program and use it wisely, and, so far, we are moving in the right direction.

The other barrier could be a shortage of funding. We do not have that shortage now. We are adequately funded, but we are hoping to see those funds remain.

I would like to give you results very quickly.

The program has been in effect for 21 months. We have 19 banks in the program. There are 50 banks, approximately, in the State. My estimate is there are 30 banks that really are in the market for this program. We are up to 19.

I am hoping to see 22 or 23 by the end of this year in the program. One of my roles is to market the program and, hopefully, get the banks in.

The number of loans—113 loans have been made to date over those 21 months. That is roughly 8 to 10 loans currently being made a month. I see that doubling over the next year because of the entry of new banks and because of the education curve as they learn how to use the program.

We have $2,700,000 out now in these 113 loans. The smallest is $2,500, the largest $175,000, out to 15 years, and the shortest loan 3 months. So, you can see how diversified the program is.

I think, importantly, 35 percent of those loans have gone into the severely affected communities of this State, by definition areas of the State with higher-than-average unemployment.

Typically, loans are $8,000 to $30,000; 80 percent of the loans are in the $8,000 to $30,000 category. So, we know we are hitting the market that we targeted, the small business.

Performance measurements: Most public programs of this nature, of a lending nature, you might get a leverage of private money to public money of $2 or $3 to $1. This program accounts for $16 to $1; $16 of bank money for every $1 of State money put into it.

Jobs: Unofficially, 152 jobs created out of those loans, and that works out to $1,100 of public money per job, compared to the usual $10,000 to $15,000 for other programs.

Startups: A third of the loans have been to new businesses. I think that is extraordinary. I did not expect that.

We have had claims, too, $5,000 to date, and we expect that, of course, to go up, and we hope it will go up as we see the program serve its actual purpose.

What is the outlook? Well, as I mentioned, I expect to go from 8 to 10 loans a month to double that within a year.

I expect another three or four banks in the program over the next year, and with the experience curve, I can see the size of the number of loans and the amounts of loans having been made to date at least doubling this year.

That is my presentation.

Chairman WYDEN. Very helpful.

Now, you three are going to have to be patient while we indulge Mr. Brown. Now this was always the case when he was in charge of my Portland office. We had to go looking for him when trying to start a meeting, but we have to swear Mr. Brown separately.

So, Mr. Brown, if you have no objection to being sworn, if you would raise your right hand.

[Witness sworn.]

Chairman WYDEN. I want to thank the other three panelists for indulging Mr. Brown after we could not find him, but we do welcome our friend and appreciate his participation. After Mr. Brown's testimony, we will have some questions from Ms. Furse.

TESTIMONY OF RICH BROWN, VICE PRESIDENT, CORPORATE COMMUNITY DEVELOPMENT, BANK OF AMERICA, PORTLAND

Mr. BROWN. Thank you, and I appreciate the committee's indulgence. I appreciate the invitation to be here. What I was asked to talk a little bit about and what I am happy to talk about is just a few of the things that Bank of America has tried to do in the short time it has been in the market here in Oregon.

I would start by saying that we have built a small business lending department—we call it Business Banking Department—from the ground up, because the predecessor institution which we acquired had, in essence, no business lending portfolio at all.

So, we have built this from the ground up, and the first thing I would say is we would not have invested the kinds of dollars and resources into this if we were not committed to this market.

So, I wanted to just kind of get that on at the outset.

The other thing we have done is we have gone out and we have talked to people, particularly small businesses and small business owners, and representatives of associations and such that represent small businesses, to ask the basic questions:

What are your problems in accessing capital? What are the obstacles? What can we do differently to make it easier for you to access capital?

A lot of this relates to the education process that has been mentioned on several panels, and I guess I would just want to reinforce that message, that the education piece is exceptionally important.

Part of that education, we think, gets down to the very basic levels before you start talking about a business plan or financials that a bank would want to see before we lend money.

We found that there were a lot of small business people who were just intimidated about going into a bank. It is an intimidating process.

So, one of the things that we have done—and I would like to enter this and provide it to the committee, a copy of a very short video.

It is about 10 or 15 minutes, and it is called "Banking for Business Made Easy.' This does not get into how to do a business plan or anything like that.

All it talks about is the very basic steps that a small business person might want to think about before they go in and talk to a banker and shows them how easy it is to go in and talk to a banker about the basic steps that you want to look at before you begin the process of borrowing money.

So, we took this back to the very elementary level, but it is an example of one of the steps we have taken, and I know that other institutions have done similar sorts of things.

The next thing that we heard—and it is kind of what has been reiterated here today—is that banks do not want to make smaller loans, particularly loans under $10,000, that banks only like to make big loans, and that the documentation process is too burdensome and too intimidating.

So, we have tried to develop a small business lending program that really tries to get at all those complaints, and we just introduced this program in December, and so, we do not really have any results that we can speak to, but I wanted to give you just some of the criteria that make up this loan which we have very high hopes for that will create some new opportunities for businesses looking for access to credit.

This is a loan that is $50,000 or below. So, this is a special loan that we are only looking at loans that are $50,000 and under, and, in fact, the minimum loan amount is $2,500. We will look at making a loan as low as $2,500. This program has less stringent credit criteria.

We have designed it so that they will get a decision within 5 days of receipt of their application.

You heard a number of discussions about the long waiting periods, and so, we have designed this such that the prospective borrower will get an answer within 5 business days.

The borrower will receive his or her money 1 day after approval of the loan, and we have an automatic renewal feature that avoids them having to go through the whole documentation and paperwork process over and over again every time they want to renew the process.

So, this is one example, I think, of what we have done, and I talk about Bank of America because that is what I know best, but I know there are a number of other institutions around the State that have embarked upon other efforts to try to meet the needs of the small business borrowers.

Another program that I wanted to just quickly mention is one that we have in place in Astoria, in Congresswoman Furse's district, that is a downtown commercial rehabilitation loan, and this is another one that is designed to get at some of the issues that are critical to small businesses and to localities, which is improving the appearance of the downtown core areas and, going through some of the other program goals here for this program, it provides financing in an affordable manner. These projects probably would not get done without this kind of financing, and we are trying to provide an incentive for new investment in downtown commercial proper-

ties, and we are doing this right now in Astoria, and we are looking at several other localities as well.

Basically, what we have is a maximum loan of $10,000 and a minimum loan of $2,000. We charge no loan fee, and we have the interest rate at the prime fixed rate.

We have looked at offering this program in areas where local governments have made a commitment to try to upgrade or improve their downtown area or main street area and have made a commitment to doing something, and we view this as part of a public/private partnership, and that is where we have looked to make this program available.

So, we have hopes that there might be other locations where we could do this.

One final piece of information I just wanted to pass on to the committee. I asked for some information regarding our loans in 1992 and how they were targeted, particularly from our small business department, and just for the committee's information, 46 percent of the loans that we made were under $25,000.

So, nearly half of all the loans that we made were under $25,000, and 36 percent of the loans were between $25,000 and $50,000. Only 10 percent of the loans were between $50,000 and $100,000, and only 8 percent of the loans were over $100,000.

So, we are making a real conscious effort to try to target into those smaller businesses that Ms. Suran talked about that are the bulk of the businesses in the State and have these smaller credit needs.

It is a smart business decision. You look at the numbers out there, and what a tremendous business opportunity, with just the sheer numbers of businesses that are out there.

Chairman WYDEN. Very good.

We will start with Congresswoman Furse.

Ms. FURSE. The issue I would like to ask you about is are there some particular Oregon Programs? We know we have the bottle bill, and we have the beach bill. We know we can do things better in Oregon.

Are there some particular Oregon Programs that you think work well that we can bring to this working group or that you can bring to this working group, that are unique, that could be used as models throughout the country, because that is what I would like to be working on? How do we make a model?

Your model sounds fascinating, the CDC. Can we do it in a way that will make it possible for the rest of the country, and are there some unique programs?

Mr. BROWN. I will mention briefly, and it is too bad that Sandy Cutler from the Small Business Development Center is not here, because the Oregon Bankers Association has embarked upon what I think is a unique effort with the small business development centers in Oregon, and I guess you have to realize that the Oregon Small Business Development Center Network is probably one of the best in the country.

So, we have an advantage there, but what we have been able to do is to team up with the Small Business Development Centers, and we provided some funding to them to help them purchase some computer software that they are using with their small business

clients, but, in addition, what we have done is gone in and provided training to the bankers.

There was a discussion in one of the earlier panels about educating the bankers, essentially so you have everybody reading off the same page in terms of what the expectations are, what the borrower needs to bring to the table, and what the business person needs to expect, or what the banker might want to expect from a borrower.

So, this program is, I think, unique to the State of Oregon and in the States that have significant small business development center networks might be something that could be replicated.

Mr. RAMSEY. Congresswoman Furse, I will not go into detail on what we have done with the CDC's, but I think there is more that can be done at the national level in dealing with those organizations, giving them access to funds, because they are able to leverage those dollars and do a good job of leveraging them.

There is one program—it is a housing program—that, although it is targeted for housing, I think that there is something that perhaps could be done in business development, even though we have got budget problems at the Federal level, because you may want to look at how we can get the Federal Government or SBA out of doing some of the direct lending that they are doing and provide another way to deliver those services.

We have what is called the Oregon Lenders Tax Credit, and what that does is it enables a lending institution, banks, et cetera, to loan funds to nonprofits or governmental entities at four points below market.

Then what the State does is we turn around and we give a tax credit back to the bank. So, in other words, my department is able to administer that program without having a lot of bureaucracy, because the bank is going to make the loan. They are going to be able to do a below-market interest rate for affordable housing.

If something like that was targeted in the business realm—maybe it is in areas that, instead of enterprise zones or whatever, where we have disadvantaged areas or, particularly, small businesses—the banks could get that kind of credit.

You would not have to have the bureaucracy built up to do it, because the lenders could do it and then turn around and get some kind of credit, and that is a way to deliver the services locally, locally based, without having centralization.

So, that is something I would like to see the State look at, but that is something perhaps the Federal Government could look at as a way to deliver services.

Mr. TOWNSEND. Congresswoman Furse, the capital access program, I think, does have an audience in Washington.

I understand that there have been inquiries, certainly directed at me and particularly to the State of Michigan, which was the first State up and running with the program, and I understand perhaps 9 or 10 States now have actually adopted the program, some with more success than others, but I would like to get back to something that Rich Brown mentioned a moment ago about the Small Business Development Centers that perhaps you could carry away with you.

You had an earlier comment two panels ago about borrowers coming to banks unprepared with financial know-how, perhaps with no financial understanding of their business whatsoever, and, therefore, they do not qualify for credit.

Another program I am very much involved with and direct is called the Entrepreneurial Development Loan Fund, and it makes loans up to $25,000 to start up businesses.

We require the borrower to present a business plan, and most of these people are displaced workers, they are severely handicapped people, and they are living in a depressed area of the State that qualifies for the program.

They must go to the Small Business Development Center. They must take a course in small business management. They must have a counselor who instructs them in plan development and presentation.

Only when we receive that plan, with a letter from the SBDC, do we move forward with a loan, and we still make a credit check.

It doesn't necessarily mean you qualify, but this is a way that States, for instance, can cooperate with the SBDC's, or any other type of development loan fund can cooperate with the SBDC, to make loans come true for borrowers.

Chairman WYDEN. Well, we will excuse you. You all have been a perfect kind of wrap-up.

I think my colleague's point about trying to look at some of the best in what is going on at the Small Business Development Centers, lender's tax credit, capital access projects, is the perfect way to send off our effort now to follow up in the working group.

Preparing for hearings is always hard work, but it is even harder to take the kernels and the nuggets that we heard today and follow them up. So, we are going to be anxious to work with you in the days ahead.

Thank you for your cooperation, and I think it is going to be a very, very busy few months on the issues that you have talked about. I want to see us be able to get together a few months hence and say that we were able to make a number of the best ideas we have heard about today grow and translate into opportunities for small businesses.

We thank you, and the subcommittee is adjourned.

[Whereupon, at 12:10 p.m., the subcommittee was adjourned, subject to the call of the Chair.]

APPENDIX

Opening Statement of Honorable Ron Wyden
Chairman, Subcommittee on Regulation & Business Opportunities
Hearing on Increasing Loans to Small Businesses

JANUARY 12, 1993

Good morning:

Today the Small Business Subcommittee on Regulation and Business Opportunities will examine new strategies for making available more credit and capital to Oregon's small businesses.

Recent evidence shows signs of a national economic rebound, but for Oregonians the real key is to produce new jobs that pay good wages. Too often in the past, large companies have grown by streamlining operations and actually reducing workers. For small businesses, it has been just the opposite -- growth does translate into more jobs. Clearly, the task of creating new jobs will be dramatically affected by small and mid-sized businesses.

That is especially true for Oregon. Over 90% of Oregon businesses employ fewer than 100 workers, and the State Division of Employment projects that fully 70% of the job creation in Oregon during the 1990s will come from those small and mid-sized firms.

The challenge is straightforward: Make new money available to small and mid-sized businesses, and we will grow jobs in Oregon; sit on our hands and we will lose our lifeblood.

Congresswoman Furse and I choose the growth option and want to

use this hearing to promote just this agenda.

Traditionally, the responsibility for lending to small businesses has fallen to local banks. In return for guaranteed deposits and borrowing rights, the government has expected banks to make special efforts to contribute to the economic health of the local community. Indeed, the Community Reinvestment Act of 1977 formally requires that banks demonstrate the efforts they make to meet the credit needs of the local community through loans for small business and housing.

Here in Oregon, activists working with the financial institutions have made progress on the housing side. We wish to see the same sort of progress on the small business side of the ledger.

Oregonians want a Community Reinvestment Act that is a powerful tool for local economic growth, not a paperwork nightmare for bankers or a full employment act for government regulators. Too often, the rules and standards that regulate financial practices defy reality.

For example, yesterday I spent an hour at Key Bank headquarters in Portland and saw that loan officers must fill out a virtual mountain of paperwork just to make a simple loan. And, a recent edition of Associated Oregon Industries' Business Viewpoint reports, "a customer who has a First Interstate account

in Vancouver, WA, can use an automatic teller machine (ATM) or cash a check in a First Interstate branch in Oregon to get cash, but cannot make a deposit to the Vancouver account in Oregon."

Depending on who you talk to, there are a variety of reasons why small businesses are finding it hard to get capital. The Chair takes special notice of the fact that experts have reported that in 1992, for the first time since World War II, America's banks actually invested more money in government securities than they lent to businesses.

Oregon's largest banks have performed significantly better than the national average on this issue. But records obtained by the Subcommitee from the Federal Deposit Insurance Corporation indicate that even in Oregon, the three largest banks decreased commercial loans by $272 million and increased investments in government securities by $725 million in the last year.

The fact is that what our community really needs is a new partnership to mobilize Oregon to work with the Clinton Administration to implement the President-elect's pledge to increase small business lending. Towards that end, Congresswoman Furse and I will establish a working group at the conclusion of this hearing to work for an Oregon growth agenda that the two of us can pursue with our colleagues.

We have significant tools at our disposal. The Small Business

Administration has indicated to me that they want to be an activist partner in promoting entrepreneurship. Portland State University wants to help emerging businesses. We look forward to our witnesses and the important follow up work that will lie ahead.

CFI

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BANKING NEEDS OF SMALL BUSINESSES
(Testimony before Hon. Ron Wyden and
Hon. Elizabeth Furse on January 12, 1993)

I appreciate the opportunity to participate in this hearing on a matter that is of critical importance to our economy. The availability of credit and capital for small businesses is ranked by nearly every commentator as a top priority in creating and maintaining jobs. Lack of these resources has been identified as a major cause of the loss of jobs in the last few years.

My name is Matt Chapman, and I am Chairman and CEO of CFI Bankers Service Group, Inc. We are based in Portland, Oregon, and provide computer software programs to the banking industry that facilitate and document transactions between banks and their customers. Although we are the eighth largest supplier of software applications to the banking industry, we are still a small business, with 130 employees and revenues last year slightly exceeding $15 million. My testimony today is not in our capacity as a software supplier to the banking industry, but as a small business. Today, I am happy to say, CFI is both highly solvent and very liquid, with several million on deposit with our bank at any given time and essentially no debt. It was not always so. We struggled and I believe that the structural issues facing banks and small businesses made our growth much more difficult, and much slower, than it needed to be.

1. Getting Capital.

CFI recapitalized in February 1991, obtaining a mix of capital and available debt commitments of $7.1 million. The process took almost exactly a year and cost about $400,000 in fees. We were very lucky even though we had a good story to tell, including a product line that leads the market and a stable and experienced management team. However, we were one of a very, very few capital deals that was done during that period. Most companies in our situation - growing fast and needing liquidity infusions - were not able to get what they needed. During this period, the venture capital market essentially pulled out of Oregon, with offices of long time firms closing and available capital from the remaining firms much reduced. Unless a small business could show a likelihood of exceptional returns, this avenue was not, and still is not, available to it. In our case, we turned to what are known as "mezzanine financiers," who put money into existing businesses in the hope of substantial returns, but with the further assurance of ongoing income on their investments. Again, very few companies can afford to pay for their capital in this manner.

My point is that there are few sources of capital for the business that is likely to be stable, have reasonable growth, but not take off to become another Nike or Sequent. Yet these are the businesses that provide the vast bulk of small business jobs. Sweat equity of the entrepreneurs that own these businesses can only go so far. There are ongoing needs, particularly if a business is growing, that simply cannot be met with the resources of the typical small business owner. Today, venture capital investors only want the potential superstars. Rather than invest in the "journeyman business," they now have investment alternatives with corresponding yields without the risk. There is a critical need for a cost effective capital source for the typical small business.

2. Getting Loans.

The solution most small businesses look to is the availability of loans. If the business has hard assets that can be used as collateral, then loans may be available.

What the small business typically has is a good idea for a service or product, usually some ongoing organization, and a bootstrap approach that relies on today's sales to feed today's workers. The problem is that customers don't usually pay for today's sales until tomorrow, and the business needs liquidity to cover that interim. It is even more difficult when the business grows, since the number of workers needed to get today's sales must grow, with a lag before the sales themselves will increase, and a further lag before those increased sales are turned into cash. For a small business, it actually isn't all that important what its balance sheet looks like. I realize this may be heresy, but the balance sheet primarily is of importance to large organizations that seek capital in the public markets. What matters to a small business is cash flow. If you can cash flow the growth of a fundamentally profitable business, you can get to the point where the balance sheet starts to look okay. But while you're on that quest, the existence of a positive cash flow is the single most critical factor that will determine the survival or failure of the enterprise. I submit that liquidity facilities - whether phrased as capital, loans, or whatever else - should be the focus of the financial resources made available to small business.

Unfortunately, there is again a shortage of funds available. CFI has had an excellent relationship with our bank, which is both a customer and a strong reference supporter of our products. However, even our bank was able to loan only on a percentage of accounts receivable when we were seeking bank debt. Although our cash flow was highly positive, our balance sheet was not particularly strong. Nonetheless, the bank supplied an appropriate line for working capital - liquidity - until the bank was examined and told that loans to companies such as us were considered unsafe and unsound under the examination guidelines. This was true of much of the high-tech industry in Portland. The local Business Journal was replete with stories of companies that had trouble maintaining their line of credit. Again, we were lucky. Our bank worked with us and we were, as noted above, able to obtain a very significant capital infusion that removed our need to borrow, based on a referral by the bank. Also again, others did not fare as well.

It bears noting that the current approach of the Small Business Administration is not focused on the business itself, but rather on available collateral and extreme caution. Indeed, reports suggest that their ultimate loss ratios aren't that much higher than commercial banks, indicating that they are in fact taking very little risk. For a company like ours, SBA was an essentially worthless option. Our assets consist of our people and our technology, neither of which can be bundled up and sold at action upon default.

It is clear that the standards for lending to small business have changed. In the past, the stress was on the 'character" of the borrower, along with other standards of cash, collateral, and capacity that were analyzed, but not individually determinative. Today the standards appear to be much more statistical, with little emphasis on character and considerable emphasis on the ratios and cash flows that appear in a company's balance sheet and income statement. This reduces the opportunity for a bank to support a management team that it believes in, and focuses on the balance sheet and the extent to which a particular business's income statement fits industry norms.

I do not claim to know fully the reasons for these changes. Some large portion is clearly due to the change in the regulatory climate, which puts bankers under the microscope for all of their loans. It is clearly inappropriate for the decision to be made by the regulatory agencies whether, for example, a particular bank should make loans to the high-tech industry. Yet regulators rely on ratio analysis to substitute for the judgment of the banker, since that is the primary tool they are trained to use. Bankers are expert at judging small businesses and knowing their communities. The structure should encourage banks to work with the businesses, not cut them off because of regulatory guidelines. It is odd to legislate that banks should reinvest in their community and regulate to force banks out of the very businesses that form the core of that community, especially when times get tough.

But banks also need to return to a "know your customer" mentality that focuses on the character of the borrowers. Frequent shifts of loan officers, changes in strategic direction of bank loan portfolio goals, and a lack of focus on the customer's needs also are a part of the problem. But the biggest need is for a return to a regulatory system that lets banks declare what small businesses to support.

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